BUY ALERT: TSX Bank Stocks Open the Profit Floodgates!

Description

Canadian banks are starting to walk off their COVID-19 damage. That's the big takeaway from a slew of quarterly reports released last week, which showed strong sequential growth. While earnings remain down year-over-year, **TSX** banks are growing compared to the prior quarter. These results were made possible by a reduction in provisions for credit losses (PCL), which sent earnings higher. As a result of the higher earnings, bank stocks are starting to look like good beaten-down post-pandemic plays.

Why bank profits popped in Q3

In Q3, bank earnings increased over Q2 for a number of reasons.

First, most banks reduced their PCL in Q3. "PCL" refers to anticipated loan losses. These losses are estimated by the banks and reported on the balance sheet. They also lower net income–but do not represent a true cash loss. If a bank raises its PCL and then lowers it later, earnings will decrease and then increase, in that order.

That's what we saw in **Toronto-Dominion Bank's** (TSX:TD)(NYSE:TD) Q3 report. In the third quarter, TD reduced its PCL from $3.2 billion to $2.2 billion, resulting in EPS increasing from $0.8 (Q2) to $1.21 (Q3) — a pretty big jump in earnings. The bank's earnings also benefitted from a record $442 million profit in wholesale banking–an increase of 81% year over year.

It was a similar story with **Royal Bank of Canada** (TSX:RY)(NYSE:RY). In Q3, RY decreased PCL by $2.1 billion compared to Q2, contributing to a $1.7 billion earnings jump. Earnings were also helped by a record $949 million profit in Capital Markets–up 45% year-over-year.

RY's overall earnings in Q3 were only down 2% year over year. That's in stark contrast to TD, which reported strong sequential growth but a pretty weak showing compared to the prior year quarter.

Will the turnaround continue?

It’s one thing to say that banks did well in Q3, but quite another to predict that the growth will continue. April, May and June saw a fairly rapid re-opening after the initial COVID-19 lockdowns. It’s unlikely that the re-opening will continue at the same pace in the coming months. Recently, there have been reports of a second wave in BC, and most provinces are opting to keep some lockdown measures in place. So, banks face less COVID-related risk factors than in Q2, albeit still more than last year.

That said, the banks’ Q3 earnings were broadly encouraging. RY is already basically flat year-over-year, and TD isn’t too far behind. It will be interesting to see how TD’s U.S. retail business fares in the next few quarters, as its earnings in that segment are down significantly more than its other businesses. That’s a pretty important one to watch because U.S. retail is TD’s biggest historical growth driver.

Foolish takeaway

If you ever thought Canadian banks were beaten down too much in the COVID-19 market crash, your confirmation is here. Across the board, revenue is holding up well and PCL are being justifiably reduced on fading risk factors. We’re not out of the woods yet, but the big banks could be good buys at today’s prices.

CATEGORY

1. Bank Stocks
2. Dividend Stocks
3. Investing

TICKERS GLOBAL

1. NYSE:RY (Royal Bank of Canada)
2. NYSE:TD (The Toronto-Dominion Bank)
3. TSX:RY (Royal Bank of Canada)
4. TSX:TD (The Toronto-Dominion Bank)

PARTNER-FEEDS

1. Business Insider
2. Koyfin
3. Msn
4. Newscred
5. Sharewise
6. Yahoo CA

Category

1. Bank Stocks
2. Dividend Stocks
3. Investing

Date
2025/08/25

Date Created
2020/09/01
Author
andrewbutton