Royal Bank of Canada (TSX:RY) Stock: A Clear Buy Post-Earnings

Description

Royal Bank of Canada (TSX:RY)(NYSE:RY) released earnings today. The stock was up 0.94% the day before the release. The bank beat on earnings but missed on revenue. Overall, it was a strong report that re-affirmed Royal Bank's status as a top-tier Canadian dividend play.

A 20% earnings beat

Royal Bank of Canada's earnings came in at $2.23 per share. That was up just 1% year over year but 20% ahead of analysts' estimates. Earnings were down considerably in personal/commercial banking but bolstered by results in capital markets and investor/treasury services. This is similar to Royal Bank's earnings in the third quarter, which also saw worse results in commercial banking than in capital markets.

Royal Bank's earnings breakdown is about what you'd expect. Commercial banking is more heavily affected by the current COVID-19 environment, because it gets hit harder by low interest rates and less commercial activity. Capital markets actually benefits from market volatility because that leads to more trading. Interestingly enough, provisions for credit losses (PCLs) in Q4 was actually lower than in Q4 of 2020. This contributed positively to earnings in commercial banking.

PCL lower than expected

Royal Bank's PCLs in Q4 was far lower than expected. The markets expected about $700 million in total PCLs. In fact, PCLs were only $427 million. This might be the one area of concern in Royal Bank's Q4 earnings. The bank's $427 million in Q4 PCLs was lower than in many pre-pandemic quarters. Yet with the second wave of COVID-19 sweeping the nation, we'd imagine that risk factors are on the rise. It's therefore possible that Royal Bank's Q4 PCLs were too low, though I'm not going to claim that I know the bank's risk factors better than its own analysts.

A generous yield

Following Royal Bank's Q4 earnings beat, its 4.04% dividend yield is looking both high and sustainable. Even with all the COVID-19 damage sustained this year, RY only has a 0.55 payout ratio. That's not bad. Royal Bank's recent dividend declaration was $1.08, which was not an increase but not a decrease either. Overall, it was a pretty prudent move by the bank's management.

By the way, Royal Bank's fourth-quarter earnings came alongside some fairly encouraging full year earnings. For the full year, RY's earnings were down only 11% — despite a whopping [$2.5 billion increase in PCLs]. This suggests that the Royal Bank will be able to get back to positive growth rates as soon as the pandemic is over. PCL hikes take a bite out of earnings. Without this year's rise in PCLs, RY's earnings would have been very solid.

The bottom line is, if you're a dividend investor, Royal Bank is a solid high-yield pick to consider. Its earnings are down this year but much less so than other banks. With a modest payout ratio, the yield is very sustainable. It's one of the better bank plays out there.

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andrewbutton