



Move Aside Big Five Canadian Bank Stocks!

Description

The Big Five Canadian banks have been anchors of diversified stock portfolios. After all, they have made consistent dividend payments that increase in most years.

These dividends provide a more attractive income than what the market offers. Particularly, the Canadian stock market yields about 2.8%. In comparison, the Big Five Canadian banks offer an average yield of 4.1%, which is 46% greater.



Total Return Level data by YCharts.

Other than income, the banks beat the market in long-term total returns as well. Leading the pack in

the 10-year total returns are [Toronto-Dominion Bank](#) and **Royal Bank of Canada**. However, the sixth-biggest Canadian bank, **National Bank of Canada** ([TSX:NA](#)) leaves both in the dust, beating them both by about 60%.

That is, over the last 10 years, the same investment in TD or RBC stock that produced \$10,000 of returns would result in about \$16,000 when invested in National Bank stock instead.

National Bank's total returns precisely demonstrate the power of compounding. Even when a stock outperforms another by only a few percentage points, they add up and make a big difference over time.

Let's take a closer look at National Bank to see how it fared against the pandemic last year.

National Bank stock during a time of high uncertainty

In fiscal 2020, most of the big Canadian banks saw a meaningful reduction in their earnings. The reduction was due to higher provisions for credit losses (PCL) as the banks set aside more cash in expectation of higher percentages of bad loans (for which most did not materialize).

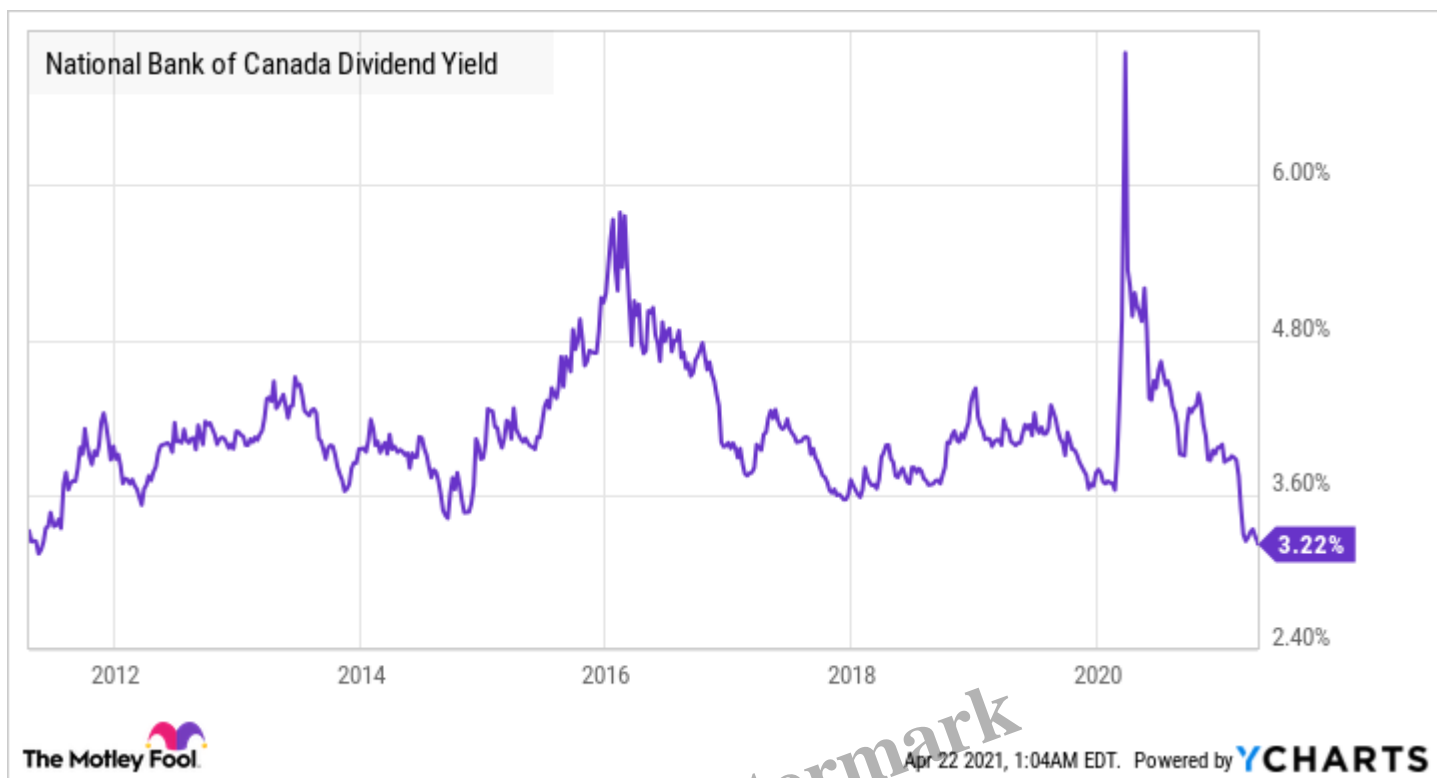
National Bank's fiscal 2020 PCL was \$846 million, up from \$347 million in fiscal 2019. However, the fiscal 2020 PCL ratio was 0.53% (up from fiscal 2019's 0.23%) versus PCL on impaired loans of 0.23% (up from fiscal 2019's 0.21%). At the same time, it grew average loans and acceptances by 7% to \$159 billion.

This compares to the largest Canadian bank as follows. [RBC's](#) fiscal 2020 PCL was \$4.35 billion, up from \$1.86 billion in fiscal 2019. The fiscal 2020 PCL ratio was 0.63% (up from fiscal 2019's 0.31%) versus PCL on impaired loans of 0.24% (down from fiscal 2019's 0.27%).

In other words, National Bank's PCL on impaired loans was even lower than RBC's last year! This implies that despite National Bank's smaller size and goal to grow, it did not trade growth with quality. Instead, it maintained a high-quality loan portfolio.

Should you buy National Bank stock today?

Currently, at \$88.22 per share, at writing, National Bank stock is fairly valued and yields 3.2%. The yield is a bit low compared to its historical levels.



NA Dividend Yield data by YCharts.

However, its yield can quickly increase in a correction or when it's allowed to increase its dividend again. Because of the highly uncertain economic environment today, regulators have banned the big Canadian banks from increasing their dividends.

National Bank's quarterly dividend has maintained the same for six quarters so far, whereas, before the pandemic, it increased its payout every six months or so.

As a result of the bank's frozen dividend and sturdy earnings, its payout ratio is estimated to be roughly 37% this year. I wouldn't be surprised if National Bank gave a big boost to its dividend once the ban is lifted.

If you're underweight in Canadian banks, consider buying a small position here. If not, certainly look into buying National Bank stock next time there's a correction in the big Canadian bank stocks.

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