Why Big Banks May Be a Great Big Bet Today

Description

Canadian banks are turning it around royally (no pun intended). Despite concerns about the recovery of the banking sector, the Big Six are performing exceptionally well. Provision for credit losses continue to go down every quarter. Additionally, improving interest rates and more than adequate liquidity ratios make these banks highly sought after as value plays right now.

In this regard, I believe **Canadian Imperial Bank of Commerce** (TSX:CM)(NYSE:CM) and **Royal Bank of Canada** (TSX:RY)(NYSE:RY) are two of the best picks investors looking at the banking sector should consider right now.

Let's discuss why this is the case.

Patience is a key virtue

Those who have been patient with big banks this past year have done very well for themselves. Indeed, I think a degree of patience is required to own these stocks over the long term.

Investors may be getting antsy with bank stocks due to the lack of dividend increases from these companies of late. Of course, the Office of the Superintendent of Financial Institutions (OSFI) has put a hold on all buybacks and dividend hikes until the economic picture becomes clearer. With things clearing up substantially of late, some expectations are that we could see Canadian banks follow their U.S. cousins in increasing their dividends dramatically in the quarters to come.

That said, OSFI chief Peter Routledge is suggesting investors remain patient for a little longer. It appears the loosening restrictions on dividend hikes and share buybacks may take some time to materialize.

Indeed, OSFI is waiting to be certain that the country has put behind the threats to its financial stability. Indeed, he agrees there is a massive improvement in this regard. But he also says that now is not the time to consider redistributing capital to shareholders quite yet.

In response to the pandemic, OSFI's former chief Jeremy Rudin swiftly made changes to bar share buybacks and dividends back in March 2020. He also lowered the Domestic Stability Buffer (DSB), which is an essential financial cushion to large-scale lenders. Lowering it to one would help encourage lending activity and prevent lending from stopping altogether.

However, now it is planning to increase the DSB to 2.5% of risk-weighted assets, effective from October this year. That said, OSFI refuses to comment on a deadline or definitive criteria that can help make a prediction as to when this uncertainty gets over.

Bottom line

Both Royal Bank and CIBC are two lenders with solid balance sheets. Both companies have reported impressive quarterly results, and show the ability to raise dividends, once allowed. Indeed, I think once the starting pistol is fired, it will be a race to see who can increase its dividend the fastest.

However, until that time comes, investors will need to be patient. I think investors should be pricing in dividend hikes in advance of any announcements right now and expect some significant income distribution growth. However, until said growth materializes, investors will note that current yields are likely to decline as capital appreciation takes over.

I think there's more room to run in financials right now. That said, this is an asset class with risk, just like any other. Investors should remember to consider holding well-diversified positions to limit downside risk from any one particular sector.

CATEGORY

1. Bank Stocks
2. Dividend Stocks
3. Investing

POST TAG

1. Bank stocks
2. banking
3. dividend
4. dividend stock
5. growth
6. growth stocks
7. market
8. Stocks

TICKERS GLOBAL

1. NYSE:CM (Canadian Imperial Bank of Commerce)
2. NYSE:RY (Royal Bank of Canada)
3. TSX:CM (Canadian Imperial Bank of Commerce)
4. TSX:RY (Royal Bank of Canada)

PARTNER-FEEDS

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

Category

1. Bank Stocks
2. Dividend Stocks
3. Investing

Tags

1. Bank stocks
2. banking
3. dividend
4. dividend stock
5. growth
6. growth stocks
7. market
8. Stocks

Date
2025/08/13
Date Created
2021/07/18
Author
chrismacdonald