Fearless Forecast: Pent-Up Dividend Increases of Bank Stocks in 6-12 Months

Description

All the Big Six bank stocks advanced on August 10, 2021, when the TSX pared down its losses from the previous day to post a new record high. The financial sector, led by bank stocks, is the third top-performing sector thus far in 2021. Investors are upbeat and awaiting the next moves of the Office of the Superintendent of Financial Institutions (OSFI).

Potential upside looms, because the country's financial regulator might lift the suspension on dividend increases and share buybacks. ABC Funds' portfolio manager, Irwin Michael, predicted in February 2021 that there would be pent-up dividend increases over the next six to 12 months.

We're on the sixth month since the forecast, although the OSFI shows no signs of moving just yet. If it lifts the suspension soon, **Royal Bank of Canada** (TSX:RY)(NYSE:RY) and **National Bank of Canada** (TSX:NA) might be the first to make shareholders happy.

Luxury to accelerate organic growth

When the big banks, including Canada's largest lender, RBC, brought down their provision for credit losses (PCLs), the levels of excess capital soared dramatically. As of the end of Q2 fiscal 2021 (quarter ended April 30, 2021), RBC had $9.9 billion more cash in the war chest.

Dave McKay, RBC's CEO, confirmed that the $185.77 billion bank has enough excess capital and internal growth to increase its dividends and do share buybacks. Management could decide to do both once the OSFI lifts the restrictions. Unlike **Toronto-Dominion Bank**, RBC isn't too keen on M&As.

According to McKay, RBC is highly focused and very picky in its acquisition strategy. He added, however, "It's great to have the luxury to see accelerated organic growth to increase our dividend based on current core earnings, and to return increasingly excess capital to our shareholders."

The blue-chip stock trades at $130.36 per share and currently pays a 3.31% dividend. Also, it outperforms the TSX year to date (+28.18% versus +17.57%). RBC is a must-own asset that can survive economic downturns.

Enough leeway to raise dividends

Canada’s sixth-largest bank, National Bank, offers a decent 2.92% dividend and trades at $97.30 per share. Likewise, current investors are content with the 37.98% gain. The payout ratio of this $32.83 billion bank is only 38.27%. Hence, it has enough room to grant a dividend increase to shareholders. The excess capital is $1.1 billion.

National Bank will present its Q3 fiscal 2021 results later this month. In the previous quarter, management reported a 111.35% increase in net income versus Q2 fiscal 2020. Besides the substantial reduction in PCL, most of its business segments reported significant increases in total revenues.

Louis Vachon, NA’s president and CEO, said, “With an industry-leading ROE, strong capital levels and prudent allowances for credit losses, we are well-positioned to selectively seize growth opportunities as we gradually exit the pandemic.”

Best assets to own

The anticipated deterioration of loan portfolios and increase in delinquencies did not happen. RBC and National Bank, along with their industry peers, have enormous cash to implement dividend increases. However, the timetable depends on OSFI’s assessment of the situation.

For Canadian households, the stay-at-home directives and work-from-home environment brought down or curtailed spending. If you have excess cash, too, now is the time to invest in bank stocks. Huge dividend increases are coming.

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