Bank Stocks: 25% Dividend Hike in 2022?

Description

The big banks continues to impress investors thus far in fiscal 2021. All of them raised their provisions for credit losses (PCLs) last year and sacrificed profits. The banking sector anticipated delinquency buckets to fill up due to clients' financial hardships caused by the pandemic.

In March 2020, the Office of the Superintendent of Financial Institutions (OSFI) ordered banks to hold share buybacks and dividend increases in abeyance. The result was a capital pile-up. OSFI's mandate remains in effect as of this writing. However, once the banking regulator lifted the restrictions, dividend investors will be thrilled.

Firewall is down

Since the wave of loan defaults didn't materialize, the firewall came down. After fiscal Q2 2021 (quarter ended April 30, 2021), the big banks had $40.5 billion in excess common equity tier one (CET1) capital. Hamilton Capital Partners said the country's top lenders are now "among the best-capitalized banks globally."

According to the investment firm, the big banks could raise their dividends by 20-25% when it gets the green light. Hamilton Capital added, "There has literally never been a time in Canadian bank history where the sector was in a stronger position to pay dividends."

Solid income growth

Toronto-Dominion Bank (TSX:TD)(NYSE:TD) has $14.6 billion in excess capital above the 11% industry-standard floor. Bharat Masrani, TD's CEO, said Canada's second-largest bank would consider returning capital to shareholders. It could also deploy capital for M&As.

As of October 25, 2021, the share price is $89.54 (+29.4%), while the dividend yield is 3.53%. In Q3 fiscal 2021 (quarter ended July 31, 2021), net income growth of TD's Canadian and U.S. retail segments was 68% and 92% versus Q3 fiscal 2020. Meanwhile, net income after three quarters reached $10.5 billion — a 55.8% increase from the same period in fiscal 2020.

The latest from TD is its foray into the robo-advisor space through TD Automated Investment Plus. Management believes it has the size to compete with fintech companies offering financial products.

Well-diversified business model

Bank of Nova Scotia (TSX:BNS)(NYSE:BNS) is the top choice of yield-hungry investors, because it pays the highest dividend among the Big Five banks. The bank stock trades at $82.36 per share (+25.51% year to date) and offers a lucrative 4.37% dividend.

Canada's third-largest bank had $5.2 billion in excess CET1 at the end of Q2 fiscal 2021. Like TD, BNS's dividend track record is more than a century. The excess capital is unheard of, says its analyst, Meny Grauman. He added, "The economy has held up a lot better than what anyone expected."

Regarding the strong results in the last three quarters, BNS president and CEO Brian Porter credit the well-diversified business model. The momentum should continue as the economy reopens fully. Lastly, BNS is the ideal retirement stock for Canadians who want to fatten their nest eggs. The payouts should be lasting like pensions.

Higher dividends are coming soon

OSFI head Peter Routledge said in June 2021 that financial uncertainty was diminishing, but it wasn't ready to allow payout increases by banks. For Hamilton Capital Partners, the lifting of restrictions should have happened two quarters ago. According to the investment firm, banks can temper the growth in capital levels by hiking dividends some more. Thus, it's an excellent time to take positions in bank stocks, particularly in TD and BNS.

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