



## 1 Big Headwind Investors in Bank Stocks Should Price In

### Description

Investors are facing a difficult environment where inflation and its impact on supply chains have been stubborn. Add to this Russia's invasion of Ukraine, which has led to a surge in the prices of commodities like oil. Indeed, the result is more uncertainty for investors.

Bank stocks have often been viewed as a hedge to these market headwinds. Rising inflation tends to boost the profit margins of major banks. While slowing growth may be a headwind, investors may want to take advantage of the money-printing nature of Canada's largest banks.

That said, there is one headwind investors should be aware of that may impact the value of Canadian bank stocks moving forward. Let's dive in.

### Power-sharing agreement with the New Democrats

Justin Trudeau recently struck a deal with left-wing New Democrats, which will keep him in power till 2025. The striking of this power-sharing agreement has other significant implications. For bank stocks, this deal is one that may be a big negative for Canadian bank stocks.

Specifically, as part of this deal, the Liberals appear ready to impose a surtax on the profits of major Canadian financial institutions. This move appears to be closer to reality than ever before, despite being previously discussed.

The ultimate impact on the return on equity or earnings growth for Canadian bank stocks remains to be seen. However, most investors are reading between the lines with this rhetoric. Should some surtax be imposed, it's likely to remain sticky. Accordingly, investors in bank stocks, particularly those in Canada, may be more wary than usual right now.

### What about Royal Bank of Canada stock?

**Royal Bank of Canada** ([TSX:RY](#))([NYSE:RY](#)) stock appears to be an attractive one right now. Indeed,

there are reasons for this optimism among bulls.

Royal Bank is the largest bank in Canada. This is also one of the most profitable banks in the mega-cap space globally. Accordingly, while a profit tax may be on the horizon, it's feasible that Royal Bank could handle such a tax with relative ease.

That said, it's hard to ignore the potential impact this move may have on the company's EPS growth moving forward. Thus, the potential for a valuation adjustment over the medium term may hurt the attractiveness of Royal Bank as a place to put fresh capital right now.

## Bottom line

Mr. Trudeau said at a news conference that the surtax implementation stays a priority. For investors in bank stocks such as Royal Bank, this is something to consider.

Investment analyst Nigel D'Souza forecasts that such a surtax will cause a 1-2% impact on the bottom lines of big banks. And while that indeed looks "very manageable" for Canadian banks, it's likely to be meaningful for investors, at least in the short term.

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