Income Investors: Are Canadian Banks Must-Buy Stocks Ahead of a Recession?

Description

Income investors don't always get opportunities to pay a bit less to get slightly more yield from the Big Six Canadian banking giants. Sure, the magnitude of risk has increased, as the macro uncertainties have surged. That said, resilient bank stocks tend to make it through the inevitable tough times.

They're built for long-term success, with robust capital ratios and the ability to continue raising dividends as provisions creep higher. Banking can be a tough business. Fortunately, Canadian banks have some of the best managers on the planet. They've been through recessions before, and although share prices have taken a hit, it tends to be the banks that are the first to rise once the bull is ready to run into the next economic expansionary cycle.

As loan growth sours, banks could tumble at a similar rate as the broader TSX Index. With many experts expecting a short-lived (or mild) recession for 2023, a 50% or 60% haircut seems unlikely for the Canadian bank stocks this time around. Further, oil and gas (O&G) strength and Bank of Canada rate hikes could help dampen any downside from a coming economic contraction.

The banks are stronger than you think!

Higher interest rates could weigh on the economy. However, they can also help give the top bank stocks a bit of relief on the margin front. If rates stay elevated and the economy can find its footing again, it's the banks that could be the first to correct to the upside en route to new all-time highs.

For now, investors are jittery over the recession. While the banks could fall further into a bear market (that's a 20% drop from peak to trough), I'd argue the recovery could be much sharper than most other stocks in Canada. Indeed, loan growth can come surging back once the recession passes.

Long-term investors should embrace such deep dips in bank stocks. Yields tend to swell, and risks may not be nearly as high, given the price one will have to pay on such dips.

Though Canadian banks may or may not be timely buys right here, I think they're terrific plays for long-term investors intending to hold for at least 10 years. We may not be at the bottom yet, but if you seek more yield for less, now is as good a time as any to start doing a bit of buying.

A bargain to bank on this summer

Bank of Montreal (TSX:BMO)(NYSE:BMO) is one of my favourite bank buys this summer. It has solid O&G exposure that should help keep the bank stock ahead of its peers in a downturn. Further, the incredible managers will be busy creating value from its Bank of the West acquisition.

BMO may not be a banking giant, but it's one of the best-run banks in North America, in my opinion. The stock trades at 6.88 times trailing earnings, with a 4.44% dividend yield, making it a bountiful bargain for any Canadian income investor who's still bullish on the banks.

Now, BMO is not immune from headwinds. However, I'd be willing to bet that BMO will make it through a 2023 recession with its long-term fundamentals fully intact.

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