What Investors Should Know About Bank of Nova Scotia's Latest Results

Description

The **Bank of Nova Scotia** (TSX: BNS)(NYSE: BNS) reported second quarter results last week. By most measures, the performance turned in by Canada's third-largest bank surpassed analysts' expectations.

Compared to the same period a year earlier, revenue increased 10%, net income grew 14% to $1.8 billion, and diluted earnings per share rose an impressive 14%, up $0.17 to $1.39 per share. The bank also delivered return on equity of 16.3%, a slight deterioration from the same period a year earlier. For comparison, **Canadian Imperial Bank of Commerce** (TSX: CM)(NYSE: CM) has the best return on equity of Canada's big five banks at nearly 22%.

Now that the dust has settled on earnings season for Canada's major banks, let's dig a little deeper and extract a few key takeaways from the Bank of Nova Scotia's most recent quarter.

Balanced growth across most segments

Most segments delivered solid growth, particularly Canadian banking and global wealth and insurance. That's good because these two divisions account for just over 50% of earnings.

Net income for Canadian banking was up 12% year over year, driven by solid loan growth — the bank registered double-digit volume increases in both credit card and consumer auto loans.

However, provisions for credit losses, or PCL, increased slightly during the quarter. This is nothing to be too concerned about at this stage, but it was a bit of a surprise and something analysts and investors will be watching closely in upcoming quarters.

Global wealth and insurance also enjoyed a strong quarter with earnings up 11% year over year, driven almost entirely by a strong performance in the wealth management segment. Assets under management grew a remarkable 18%, driven by the addition of new clients and portfolio growth among existing clients. The bank earns a small percentage, annually, based upon the amount of assets it manages on behalf of clients — more assets means more income.

But no growth in international banking

Despite the overall strong quarter, the performance of its international banking segment was surprisingly weak.

The Bank of Nova Scotia is the most international of Canadian banks, and is viewed by many investors as a conservative way to gain some emerging market exposure. The international banking segment is the second most important for the bank, and accounted for 26% of second-quarter earnings.

However, earnings growth was basically flat for the segment compared to the same period a year earlier. Strong deposit and loan growth, of 16% and 14% respectively, was offset by lower net interest margin and higher provisions for loan losses among business customers. Net interest margin, or NIM, measures the difference between interest income earned on loans and interest paid to lenders for deposits. The higher the better, at least from investors' and the bank's perspective — not so much for customers.

Increased potential for acquisitions

The market was surprised when Bank of Nova Scotia announced plans to divest most of its 37% stake in **CI Financial** (TSX: CIX). With over $97 billion in assets under management, CI Financial is one of Canada's top asset managers.

Given Bank of Nova Scotia's focus on growing its wealth management business internationally, as opposed to within Canada, the move shouldn't be a complete surprise. Canadian banks in general are sitting on excess capital, and once it sells the majority of its stake in CI Financial, worth $2.3 billion-$2.6 billion, it will be in an excellent position to drive growth internationally through acquisitions, particularly in its wealth management business.

An emerging opportunity

The Bank of Nova Scotia offers investors a fairly valued stock, and a dividend yield of 3.7%. In addition, and of particular importance to long-term investors, it provides a relatively low-risk way to gain emerging market exposure. It targets countries that have sound economic policies, a growing middle class and an increasingly educated population. Over the long term, the Bank of Nova Scotia should benefit as growth in these economies accelerates.

CATEGORY

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