WEEKLY
# MARKET INSIGHTS

May 29th, 2016

THE LATEST MARKET INSIGHTS
FROM THE RICHARDSON GMP TEAM

## Canadian Banks

It's been a busy week for most of Canada's major banks as four of the "big six", with the exception of Bank of Nova Scotia and National Bank, reported their fiscal second quarter earnings of 2016 reflecting operations from February through April. Bank of Nova Scotia will report on Tuesday, May 31, while National will report the following day on June 1. Overall we believe the results thus far can be characterized as "better than expected" with analyst expectations. We noticed a few trends amongst the first four banks that will likely continue with Scotia and National, which include the following.

First the oil and gas sector was at the forefront. It was only a matter of time before banks started to accelerate provisions taken for bad loans in this sector due to the decline in underlying energy prices since mid-2014. More importantly, the action taken by the banks was expected and therefore did not come as a surprise. In fact, based on the share price responses to the earnings, one could conclude that the increased provisions/impaired loans were in line or even better than expected in some cases. That is not to say that the banks are in the clear when it comes to their resource related loan portfolios, but it does signal that risk is manageable at this point in time.

The increased specific loan loss provisions affected capital market/wholesale earnings in particular, but some of that weakness was offset by an increase in trading activity and investment banking revenue following a poor Q1 which included the painfully slow month of January.

**Canadian Banks Q2/16 - Summary of Various Metrics**

| | Reported EPS | Average Estimate | LLPs ($Millions) Q2/16 | Oil & Gas LLPs ($Millions) Q2/16 | Oil & Gas LLPs ($Millions) Q1/16 | Oil & Gas Impaired Loans Q2/16 | Oil & Gas Impaired Loans Q1/16 | % of Oil & Gas Portfolio Impaired |
|---|---|---|---|---|---|---|---|---|
| Bank of Montreal | $1.73 | $1.74 | 201 | 31 | 12 | 410 | 162 | 5.6% |
| CIBC | $2.40 | $2.35 | 324 | 81 | 24 | 708 | 128 | 11.1% |
| Royal Bank | $1.71 | $1.64 | 460 | 115 | 106 | 1040 | 310 | 13.0% |
| TD Bank | $1.20 | $1.16 | 584 | 49 | 11 | 211 | 86 | 3.2% |

LLPs = Loan Loss Provisions

Source: Company Reports


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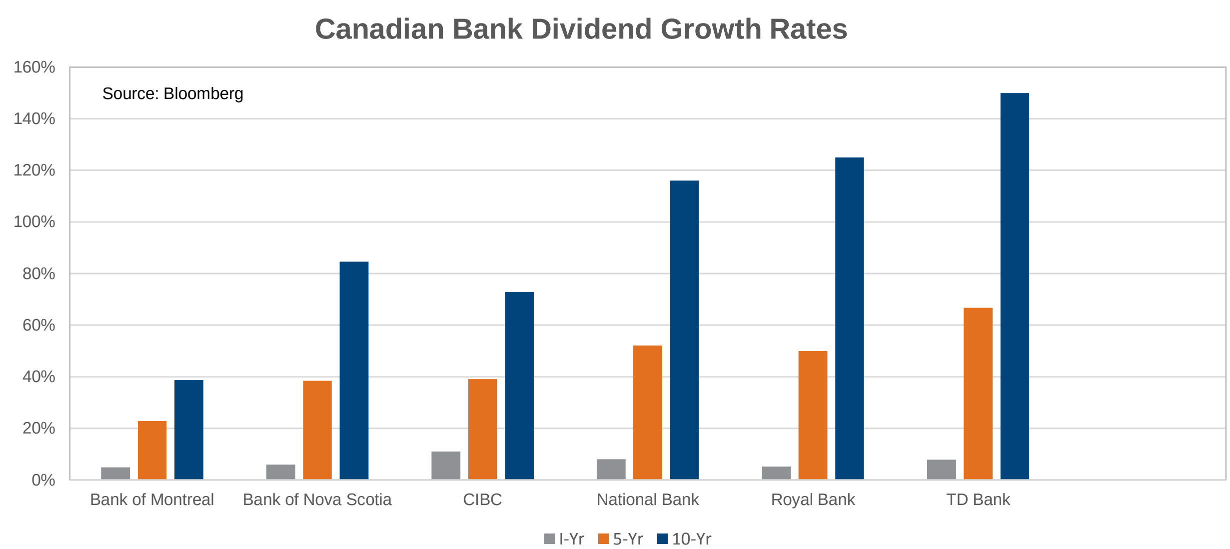
## Banks

Second, we'd note that the backbone Canadian personal and commercial banking platforms remain stable for the banks that have reported thus far. All four banks reported increased earnings year-over-year even though net interest margins were flat or fell over the past 12 months which indicated results improved either through lowering costs or driving higher loan and deposit volumes. The same can't be said when we make a comparison to last quarter as Royal Bank was the only bank to post an improvement from fiscal Q1. The other three saw a bit of pressure either due to increased loan loss provisions or lower revenue.

Third, we saw relative strength year-over-year from U.S. retail operations (for BMO and TD) and for most wealth management divisions. The U.S. is still an area of growth for Bank of Montreal and TD Bank, while improving markets helped asset levels and fee based revenue from wealth management operations.

Finally, not so much a trend, but we did see a dividend increase from Bank of Montreal as expected, National Bank may increase its dividend next Wednesday, and CIBC did surprise us with a seventh consecutive quarterly dividend increase (ninth in ten quarters). CIBC has been playing catch up to the other banks which started raising their dividends again back in 2011. It's likely the bank will now wait a quarter or two before increasing the dividend again. TD Bank and Royal Bank were not expected to raise their dividends this quarter, nor is Bank of Nova Scotia on Tuesday.




So overall the second quarter of 2016 for the Canadian banks appears to have left investors happy for now as underlying operations remain stable and risk appears manageable in the current economic and commodity pricing environment. We don't expect a material rally from these results as most banks saw share prices appreciate going into the quarterly results.

*Charts are sourced to Bloomberg unless otherwise noted.*