Banks dole out dividends bonanza

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Canada's banks have been cautioning investors for months about a coming slowdown in profits. But they continue to defy their own words.

The country's Big Six banks earned a combined $8.2-billion in the third quarter, and unleashed a torrent of dividend increases unlike any the sector has seen in years.

Five of Canada's Big Six banks raised their payouts this week. The increases will put an additional $563-million in the pockets of their shareholders over the next year.

It was the first time in recent memory that Canada's five largest banks increased their quarterly dividend at the same time, a clear signal that Canada's banking sector remains healthy despite a long list of ongoing economic concerns hanging over their businesses, from record levels of consumer debt to a softening economy and the threat of another downturn.

National Bank Financial analyst Peter Routledge said the profits reported by Royal Bank of Canada in particular "belie our rather pessimistic outlook for Canadian personal and commercial bank earnings across the industry."

RBC, the country's largest bank and largest public company, made its highest quarterly profit ever with earnings of $2.2-billion. It boosted its quarterly payout 5.3 per cent to 60 cents a quarter.

Toronto-Dominion Bank led the way with the biggest dividend hike, a 7-per-cent increase to 77 cents, after the bank reported a $1.7-billion profit and a record quarter, driven by higher profits at its Canadian branch operations.

And Canadian Imperial Bank of Commerce booked a 4.4 per cent dividend increase to 94 cents, while also reporting a significant jump in profit to $841-million.

That parade of earnings and dividend increases came after Bank of Montreal and Bank of Nova Scotia set the tone for the third-quarter earnings season on Tuesday with dividend increases of their own. Only Canada's sixth-largest bank, National Bank of Canada, decided not to boost its payout to shareholders, even as it reported a 13 per cent increase in profit Thursday, to $360-million. But that was only because National had just recently raised its dividend last quarter.

Even though the banks have been suggesting earnings growth will likely slow in the year ahead, as demand for consumer loans moderates and Canadians pay down debt, the dividend increases indicate the financial institutions themselves are comfortable that any sluggishness will not be significant. Toronto-Dominion Bank chief executive officer Ed Clark said the increase at his bank reflects "the board's confidence in our continuing ability to deliver long-term growth even in a tough operating environment."

Mr. Clark also told analysts on a conference call that TD was stepping up its dividend targets, and expects to roll out two dividend hikes a year for the foreseeable future, “earnings growth permitting.”

When the financial crisis hit in 2007, Canada’s bank regulator suggested the financial institutions freeze all increases as a way to preserve capital for a rainy day. The banks obliged, and the next dividend increase didn’t come until late 2010 when the chill was lifted. But not all banks rushed back in. When BMO raised its payout this week, it was the first increase that bank had introduced in five years.

But even as dividends grow, bank shares have been rising slowly this year. The sluggishness comes amid persistent low interest rates, which are eating into bank profit margins – though not yet to the point where the lenders are unable to produce hefty earnings increases.

In reporting its biggest quarterly profit ever on Thursday, RBC said nearly half of its profit came from its bread-and-butter Canadian lending business. The head of that business, David McKay, told analysts on a conference call that the environment is still challenging. With mortgage rates down, “the key is to keep growing your credit card business, your commercial business, to try to offset that,” he said.

And while RBC stressed that it was stealing market share from rivals, the sector’s performance suggests that Canadians are still borrowing increasing amounts, and these loans are still paying off for the banks.