



National Bank of Canada (NTIOF)

Updated April 12th, 2021 by Kay Ng

Key Metrics

Current Price:	\$69	5 Year CAGR Estimate:	8.3%	Market Cap:	\$23B
Fair Value Price:	\$66	5 Year Growth Estimate:	6.0%	Ex-Dividend Date:	06/26/21 ¹
% Fair Value:	104%	5 Year Valuation Multiple Estimate:	-0.8%	Dividend Payment Date:	08/01/21 ²
Dividend Yield:	3.3%	5 Year Price Target	\$89	Years Of Dividend Growth¹:	9
Dividend Risk Score:	B	Retirement Suitability Score:	B	Last Dividend Increase¹:	2.2%

Overview & Current Events

National Bank of Canada (or simply National Bank) is the sixth-largest bank in Canada behind the Big Five banks with Royal Bank of Canada (RY) and Toronto-Dominion Bank (TD) leading at the top. National Bank's historical roots go as far back as 1859. Since 1993, it has maintained or increased its dividend per share every year. All figures in this report are in U.S. dollars unless otherwise specified.

The bank reported strong fiscal Q1 2021 results on 02/24/2021 with net income growth across all business segments. Against fiscal Q1 2020, it reported revenue growth of 13% to C\$2,281 million, an adjusted net income growth of 23% to \$761 million, and adjusted diluted earnings-per-share ("EPS") growth of 26% to C\$2.15. Adjusted return on equity ("ROE") rose to 21.2% from 18.3% year over year.

This bank has been more resilient than its bigger Canadian banking peers. It certainly has what it takes to weather this highly uncertain economic times during the novel coronavirus pandemic. The bank's capital position remains solid with a Common Equity Tier 1 ratio at 11.9%, up from 11.8% a year ago.

Like its bigger Canadian banking peers, National Bank's earnings have rebounded. And we provided a higher fiscal 2021 EPS estimate of US\$5.77. Besides, the bank's provisions for credit losses (PCL) as a percentage of average loans and acceptances have been relatively low compared to its larger competitors. Therefore, its adjusted earnings hardly felt a dent in fiscal 2020. Specifically, its PCL ratio was 0.53% in fiscal 2020 versus 0.23% in fiscal 2019. In fiscal Q1 2021, its PCL ratio was 0.19%. Its PCL ratio on impaired loans was 0.49% in fiscal 2020 versus 0.21% in fiscal 2019. Its fiscal Q1 2021 PCL ratio on impaired loans was 0.15%. These PCL ratios demonstrate prudent lending practices.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	\$3.44	\$3.97	\$3.95	\$3.93	\$3.51	\$3.26	\$4.23	\$4.51	\$4.81	\$4.68	\$5.77	\$7.72
DPS	\$1.35	\$1.56	\$1.60	\$1.65	\$1.52	\$1.63	\$1.77	\$1.84	\$2.00	\$2.11	\$2.26	\$3.17
Shares¹	321	323	326	329	337	338	340	335	334	336	337	346

From 2011 to 2019, excluding the 2020 pandemic year, National Bank compounded its EPS by 8.2% in CAD\$. From 2011 to 2020, in the Canadian currency, National Bank compounded its EPS by 6.3%, while its five-year EPS growth was roughly 5.2%. These are above average when compared to its bigger peers. Stellar earnings growth also led to above-average dividend growth.

With about 80% revenue exposure to Canada and 55% revenue exposure to Quebec, the bank's growth rate is tied closely to the economic health of Canada and in particular to Quebec. Quebec is the second most populous province in Canada and contributes about 20% of Canada's GDP. National Bank generates 19% of revenue from the United States and Cambodia, which help contribute to higher growth long term.

¹ Estimate

² Estimate

1. Years of dividend growth in C\$; TTM dividend per share over prior TTM dividend per share in C\$; Shares in millions.

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National Bank has proved to be quite defensive. We estimate EPS to grow 6% through 2026. The bank has maintained the same dividend for 6 straight quarters. As the macro environment continues to improve post-pandemic, especially with the vaccine rollouts, it shouldn't be long before regulators allow the bank (and its peers) to increase their dividends again. Ultimately, we think it's possible that the bank can increase its dividend by at about 7% per year through 2026.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	10.6	9.4	10.1	11.4	10.2	12.7	11.6	10.2	11.3	10.1	12.0	11.5
Avg. Yld.	4.0%	4.1%	4.0%	4.0%	4.2%	3.9%	3.6%	4.0%	3.7%	4.5%	3.3%	3.6%

National Bank has traded at an average price-to-earnings ratio of 10.8 from 2011-2020. However, the investment community has steadily discovered the bank's quality and its average P/E ratio from 2016-2020 was 11.2. We think that if National Bank continues to maintain its way of doing business and interest rates were to resume growth post pandemic, it could further expand its P/E to 11.5 by 2026. Using our 2021 EPS estimate, the bank trades at a P/E of 12.0 – which indicates a fairly valued stock.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	39%	39%	41%	42%	43%	50%	42%	41%	42%	45%	39%	41%

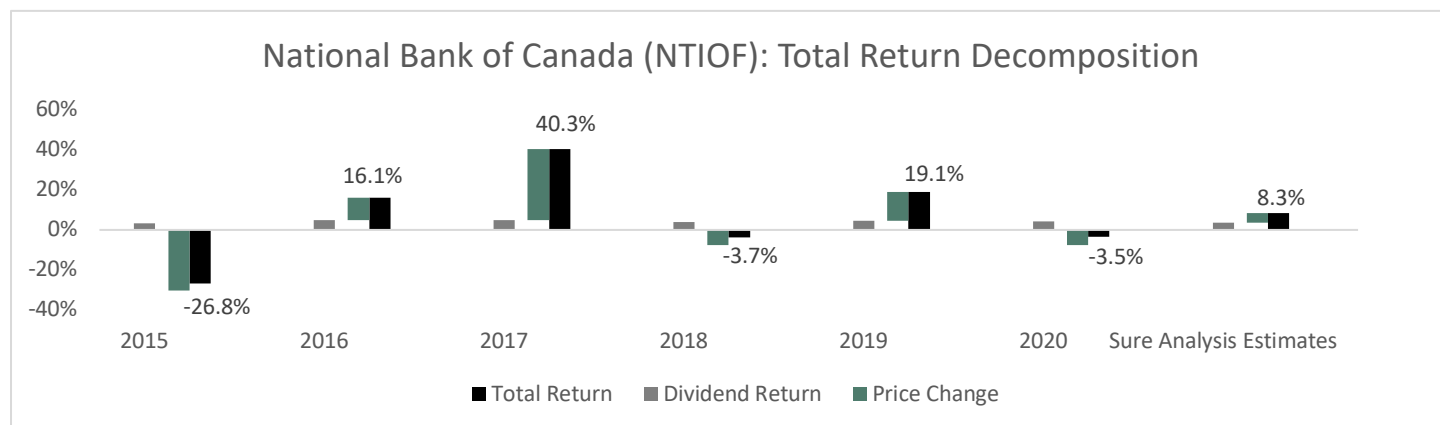
National Bank has a dominant position in Quebec. It also benefits from the effective regulation of the Canadian banking system. The World Economic Forum ranked Canada's banks as among the soundest in the world for the past decade or so, which highlights the fact that Canadian banks — National Bank included — are well capitalized and well managed.

Like all financial institutions, the bank's balance sheet primarily consists of debt, largely in the form of deposits. The Big Five Canadian banks tend to maintain a payout ratio of about 50%. So, National Bank's payout ratio is reasonable. It should keep paying its dividend as the economy makes a comeback. We believe a dividend growth of about 7% through 2026 is achievable.

Final Thoughts & Recommendation

We forecast defensive National Bank with 8.3% in total returns annually over the next five years, consisting of a yield of 3.3%, 6.0% earnings-per-share growth, and a 0.8% headwind from valuation contraction. We rate the stock a hold, but conservative investors looking for a low-risk dividend payer can consider buying the stock, especially on meaningful dips.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	4727	5259	5027	4974	4609	4393	5027	5548	5566	5876
SG&A Exp.	1752	1944	1863	1880	1741	2123	2284	2448	2481	2660
D&A Exp.	129	142	147	153	243	314	268	235	247	333
Net Profit	1240	1554	1421	1348	1248	891	1483	1667	1697	1518
Net Margin	26.2%	29.5%	28.3%	27.1%	27.1%	20.3%	29.5%	30.1%	30.5%	25.8%
Free Cash Flow	1833	1569	415	3492	3697	3899	958	4178	5851	14481
Income Tax	279	324	247	271	189	170	370	423	348	337

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	167838	177939	179561	183438	164159	173086	191617	200055	213759	248923
Cash & Equivalents	2868	3250	3431	7220	5748	6100	6861	9723	10403	21874
Accounts Receivable	2289	3046	2040	1740	1188	1480	1313	1966	1435	1576
Goodwill & Int. Ass.	1599	1841	1872	2027	1775	1902	2064	2078	2140	2138
Total Liabilities	160289	169697	171020	174060	155533	164066	181049	189114	202264	236626
Accounts Payable	3446	4302	4258	3539	2902	2148	2593	2742	2652	2452
Long-Term Debt	3523	3937	3704	2994	2220	1833	845	1357	1517	871
Shareholder's Equity	5753	6459	7143	7576	7241	7187	8340	8785	9363	10081
D/E Ratio	0.54	0.55	0.48	0.35	0.28	0.22	0.09	0.13	0.14	0.07

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	0.8%	0.9%	0.8%	0.7%	0.7%	0.5%	0.8%	0.9%	0.8%	0.7%
Return on Equity	22.6%	25.4%	20.9%	18.3%	16.8%	12.3%	19.1%	19.5%	18.7%	15.6%
ROIC	11.2%	13.4%	11.6%	11.0%	10.8%	8.2%	13.3%	14.1%	13.4%	11.6%
Shares Out.	321	323	326	329	337	338	340	335	334	336
Revenue/Share	14.39	16.14	15.37	15.02	13.84	12.92	14.58	16.16	16.49	17.41
FCF/Share	5.58	4.82	1.27	10.55	11.10	11.47	2.78	12.17	17.33	42.90

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

Disclaimer

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