



Bank of Nova Scotia (BNS)

Updated May 27th, 2023 by Kay Ng

Key Metrics

Current Price:	\$49	5 Year CAGR Estimate:	12.9%	Market Cap:	\$59B
Fair Value Price:	\$57	5 Year Growth Estimate:	4.8%	Ex-Dividend Date:	07/03/23
% Fair Value:	86%	5 Year Valuation Multiple Estimate:	3.0%	Dividend Payment Date:	07/27/23
Dividend Yield:	6.3%	5 Year Price Target	\$72	Years Of Dividend Growth¹:	11
Dividend Risk Score:	B	Retirement Suitability Score:	A	Rating:	Buy

Overview & Current Events

Bank of Nova Scotia (often called Scotiabank) is one of the Big Five Canadian banks. Scotiabank reports in 4 core business segments – Canadian Banking, International Banking, Global Wealth Management, and Global Banking & Markets. The bank stock is cross-listed on the Toronto Stock Exchange and the New York Stock Exchange using ‘BNS’ as the ticker. We’ll be using U.S. dollars throughout this report unless otherwise stated.

Scotiabank reported fiscal Q2 2023 results on 5/24/23. For the quarter, on an adjusted basis, revenue fell marginally to C\$7,929 million, while non-interest expenses jumped 10% to C\$4,555 million. Adjusted net income declined 21% to C\$2,174 million, which translated to adjusted earnings-per-share (“EPS”) falling 22% to C\$1.70, being weighed down by higher non-interest expenses and higher a provision for credit losses (PCL) that was C\$709 million versus C\$219 million a year ago. The adjusted return on equity remained acceptable at 12.4%, down from 16.4% a year ago. The bank’s capital position remained solid with its Common Equity Tier 1 ratio at 12.3%.

The fiscal year-to-date results provide a bigger picture. Adjusted revenue dropped 0.5% to C\$15.9 billion. Non-interest expenses rose 8% to C\$9 billion, while the PCL was three times year over year at C\$1,347 million, reflecting a less favorable macroeconomic outlook. The adjusted net income ended up 18% lower at C\$4,540 million, resulting in adjusted EPS that was also 18% lower at C\$3.55.

The bank increased its quarterly dividend by 2.9% to C\$1.06 per share. In light of the latest results, we lowered BNS’s fiscal 2023 EPS estimate to US\$5.32.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	\$4.84	\$4.75	\$4.28	\$4.50	\$5.10	\$5.35	\$5.39	\$4.14	\$6.15	\$6.26	\$5.32	\$6.73
DPS	\$2.34	\$2.35	\$2.18	\$2.17	\$2.33	\$2.55	\$2.63	\$2.67	\$2.85	\$3.13	\$3.11	\$3.93
Shares¹	1,209	1,217	1,203	1,208	1,199	1,227	1,216	1,211	1,224	1,191	1,197	1,258

Scotiabank’s five-year EPS growth rate was just north of 5.4% in Canadian dollars and 4.2% when converted to USD from fiscal 2017-2022. Inflation and interest rates are much higher than in the recent past, which don’t bode well for the economy, as both business and consumer spending would be dampened. Moreover, BNS could have more volatile earnings because of its exposure to international markets and different currencies. A relatively strong USD would weaken its results when translated into USD. For now, we give BNS an EPS growth rate of 4.8% (and corresponding DPS growth rate) through 2028. We set our 2022 dividend estimate based on the forex rate at writing. Keep in mind that the fluctuations in the forex between U.S. dollars and Canadian dollars will affect the effective yield for U.S. shareholders.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	12.9	11.7	9.9	13.0	12.5	10.0	11.4	9.6	12.4	10.2	9.2	10.7
Avg. Yld.	3.9%	3.8%	4.6%	4.0%	3.6%	4.7%	4.6%	6.2%	4.7%	5.1%	6.3%	5.5%

¹ Years of Dividend Growth in C\$; Shares in millions

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From fiscal 2013-2022 and 2018-2022, Scotiabank traded at an average price-to-earnings ratio of about 11.4 and 10.7, respectively. We use the more conservative P/E of 10.7 as our target due to the more negative outlook. Using our 2023 EPS estimate, the bank currently trades at a price-to-earnings ratio of 9.2, which makes the stock undervalued. BNS's yield is above average to the market, making it appealing to income investors. As a Canadian stock, BNS's dividends may be subject to a 15% dividend withholding tax for U.S. investors. This tax can potentially be avoided by investing in BNS through a retirement account.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	48%	49%	51%	48%	46%	48%	49%	64%	46%	50%	58%	58%

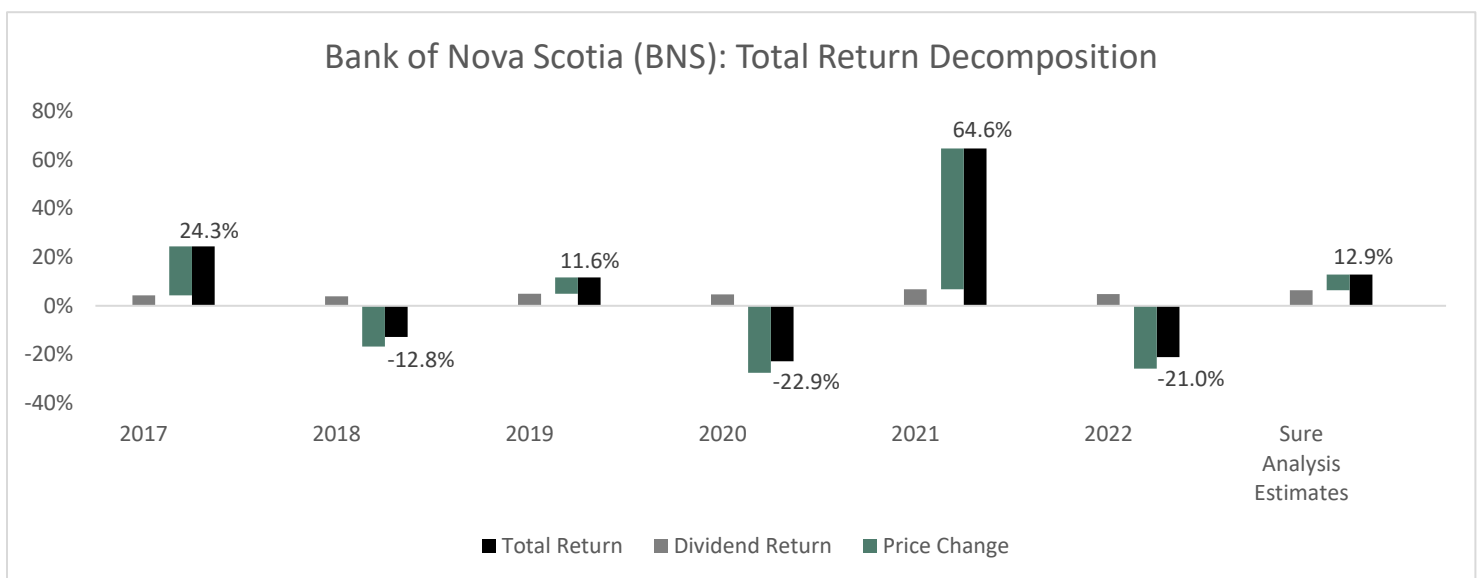
During the Great Recession, Bank of Nova Scotia increased its dividend and only froze its dividend in fiscal 2010 before resuming dividend growth afterwards. Similarly, the OSFI regulatory restriction led to a dividend freeze of 9 quarters because of the pandemic (and potential impacts to the economy). The stable bank came out with a dividend increase as soon as the ban was lifted. BNS normally has a payout ratio of around 50% that aligns with other big Canadian banks. Its payout ratio was higher than normal in fiscal 2020 due to a higher provision for credit losses from pandemic impacts. BNS's payout ratio has normalized, and we expect it to stay more or less in the 50% range.

The bank's competitive advantage is in its international growth strategy, as it is willing to acquire growth outside of its primary markets. When the global economic environment improves, its international strategy should be an advantage for growth. Scotiabank's international focus is on Latin America geographies like Mexico, Peru, and Chile. For the time being, this global strategy is weighing on its results but its juicy dividend is still sustainable from its earnings.

Final Thoughts & Recommendation

While the rest of the Big Six Canadian Banks increased their dividends in calendar Q4 2022, BNS did not. So, the market is correct to discount its valuation. We see total annual returns of about 12.9% annually in the coming years. These returns should accrue from a yield of 6.3%, valuation expansion of 3.0%, and 4.8% earnings-per-share growth. As a result, the high-yield stock earns a buy recommendation from Sure Dividend.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	20,225	21,269	19,052	19,560	20,452	21,931	22,861	23,129	24,571	24,193
SG&A Exp.	6,615	6,532	5,860	5,763	6,083	6,246	6,823	6,746	7,110	7,236
D&A Exp.	506	483	471	516	582	659	792	1,150	1,201	1,189
Net Profit	6,257	6,489	5,652	5,367	6,121	6,644	6,313	5,042	7,650	7,702
Net Margin	30.9%	30.5%	29.7%	27.4%	29.9%	30.3%	27.6%	21.8%	31.1%	31.8%
Free Cash Flow	8,607	4,283	13,009	3,158	12,680	13,520	-9,188	41,576	-10,547	12,716
Income Tax	1,704	1,837	1,493	1,531	1,554	1,851	1,860	1,148	2,282	2,142

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets (B)	709	719	651	668	713	761	825	853	956	992
Cash & Equivalents	50,884	50,657	56,161	34,545	46,506	47,461	35,482	57,392	69,655	48,419
Accounts Receivable	2,591	2,556	2,830	2,926	3,001	3,566	3,864	3,631	3,515	3,986
Goodwill & Int. Ass.	10,212	9,719	8,698	9,050	9,436	13,505	13,264	12,772	13,398	12,369
Total Liabilities (B)	666	675	610	625	665	709	772	800	897	937
Accounts Payable	7,679	6,677	5,575	5,954	6,887	7,162	6,989	6,237	7,198	9,232
Long-Term Debt	5,572	195,192	181,271	165,540	169,238	180,354	192,719	161,570	195,471	225,971
Shareholder's Equity	38,317	40,151	37,289	39,251	43,225	46,528	48,331	47,153	52,248	47,872
D/E Ratio	0.13	4.56	4.59	3.95	3.62	3.63	3.76	3.16	3.42	4.20

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	0.9%	0.9%	0.8%	0.8%	0.9%	0.9%	0.8%	0.6%	0.8%	0.8%
Return on Equity	17.0%	16.5%	14.6%	14.0%	14.8%	14.8%	13.3%	10.6%	15.4%	15.4%
ROIC	12.5%	4.5%	2.5%	2.5%	2.9%	3.0%	2.6%	2.2%	3.3%	2.9%
Shares Out.	1209	1222	1232	1226	1223	1229	1251	1243	1225	1208
Revenue/Share	16.73	17.41	15.46	15.95	16.72	17.84	18.27	18.61	20.06	20.03
FCF/Share	7.12	3.50	10.56	2.58	10.37	11.00	-7.34	33.45	-8.61	10.53

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

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