



Royal Bank of Canada (RY)

Updated December 2nd, 2023 by Kay Ng

Key Metrics

Current Price:	\$91	5 Year CAGR Estimate:	11.8%	Market Cap:	\$128B
Fair Value Price:	\$104	5 Year Growth Estimate:	5.5%	Ex-Dividend Date:	01/24/24
% Fair Value:	88%	5 Year Valuation Multiple Estimate:	2.6%	Dividend Payment Date:	02/23/24
Dividend Yield:	4.5%	5 Year Price Target	\$136	Years Of Dividend Growth¹:	13
Dividend Risk Score:	B	Retirement Suitability Score:	A	Rating:	Buy

Overview & Current Events

The Royal Bank of Canada – hereafter RBC – is the largest bank in Canada by market capitalization, and the country’s largest bank by total assets. RBC offers banking and financial services to customers primarily in Canada and the U.S. and is a member of the Big 5 Canadian banks. The financial institution operates in four core business units: Personal & Commercial Banking (39% of FY2023 revenue), Wealth Management (31%), Insurance (10%), and Capital Markets (20%). Its revenue mix is roughly 59% Canada, 25% the U.S., and 16% international.

RBC is cross-listed on the Toronto Stock Exchange and the New York Stock Exchange, trading under the ticker RY on both exchanges. All figures in this research report are in U.S. dollars unless otherwise noted.

On 11/30/23, RBC reported its fiscal Q4 and full year 2023 earnings results. Compared to the prior year’s quarter, the bank reported revenue growth of 3.7% to C\$13.0 billion. Management put aside a reserve of C\$720 million in the form of provision for credit losses (PCL) (that dragged down net income) in response to a more negative macroeconomic outlook in North America (versus a PCL of C\$381 million in fiscal Q4 2022). Additionally, non-interest expense rose 13% to \$8.1 billion. Net income ended up rising 6.4% year over year (“YOY”) to C\$4.1 billion; on a per-share basis, it rose 5.8% to C\$2.90. Adjusted net income was marginally higher at C\$4.0 billion, and its adjusted diluted earnings-per-share (“EPS”) was flat at C\$2.78. The bank’s capital position is strong with a Common Equity Tier 1 ratio at 14.5%, up from 12.6% a year ago. The bank also increased its quarterly dividend by 2.2% to C\$1.38 per share.

The full year fiscal 2023 results show a bigger picture. Revenue growth was 15%, diluted EPS fell 5%, and adjusted EPS rose 1.7% to C\$11.38, which translates to US\$8.39. The PCL on impaired loans remain low at 0.21% (versus 0.10% in fiscal 2022). Its return on equity, though, down from 16.4% a year ago, remained solid at 14.2%. We initiate the fiscal 2024 EPS estimate at US\$8.64.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	\$5.36	\$4.99	\$5.06	\$5.88	\$6.26	\$6.72	\$6.04	\$8.68	\$8.16	\$8.39	\$8.64	\$11.29
DPS	\$2.60	\$2.47	\$2.44	\$2.66	\$2.93	\$3.06	\$3.19	\$3.43	\$3.84	\$3.97	\$4.06	\$5.31
Shares¹	1,449	1,450	1,494	1,453	1,439	1,430	1,420	1,427	1,389	1,400	1,395	1,374

RBC makes strategic acquisitions to grow its business for the long haul. For example, in September 2022, it announced the completion of its acquisition of Brewin Dolphin, an award-winning wealth-management firm in the U.K., for £1.6 billion. Subsequently, in November 2022, it announced its intention to acquire HSBC Canada for C\$13.5 billion, which is expected to close in Q1 2024. From FY2014-2023, RBC increased its EPS by 7.2% per year in C\$. When translated into US\$, it was 5.1% per year. Management targets a medium-term growth rate of about 7%, but we set our estimated growth rate at 5.5% through 2029 to account for forex risk. Near-term earnings are pressured from a more negative macroeconomic outlook in the Canada and the U.S. and a higher US\$ versus C\$. Notably, during highly uncertain economic times, the federally-regulated bank may be restricted from raising dividends. RBC has a more diversified business mix than its peers, which should lead to a lower-risk, lower volatility stock.

¹ Dividend growth in C\$ based on fiscal year; Shares in millions.

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Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	13.1	12.3	11.8	12.8	13.1	11.9	11.5	12.6	12.1	11.5	10.5	12.0
Avg. Yld.	3.7%	4.5%	3.6%	3.3%	4.3%	3.9%	4.6%	3.1%	3.7%	4.5%	4.5%	3.9%

Because of the bank's size, above-average stability, and entrenched presence in the U.S. market, RBC tends to trade at a premium to its peers in the Canadian banking industry. From 2014-2023, RBC's average price-to-earnings ratio ("P/E") was 12.3 and averaged a yield of 3.9%. Its average P/E from 2019-2023 was 11.9. We think it'd be fair to target a P/E of 12.0. Using our estimate for fiscal 2024 EPS, the bank is currently priced at a price-to-earnings multiple of 10.5. So, it trades at a slight discount. RBC's yield likely won't stray far away from about 4% in the long run.

As a Canadian stock, RBC's dividends may be subject to a 15% dividend withholding tax for U.S. investors. This tax can potentially be avoided by investing in RBC shares through a retirement account.

Safety, Quality, Competitive Advantage, & Recession Resiliency

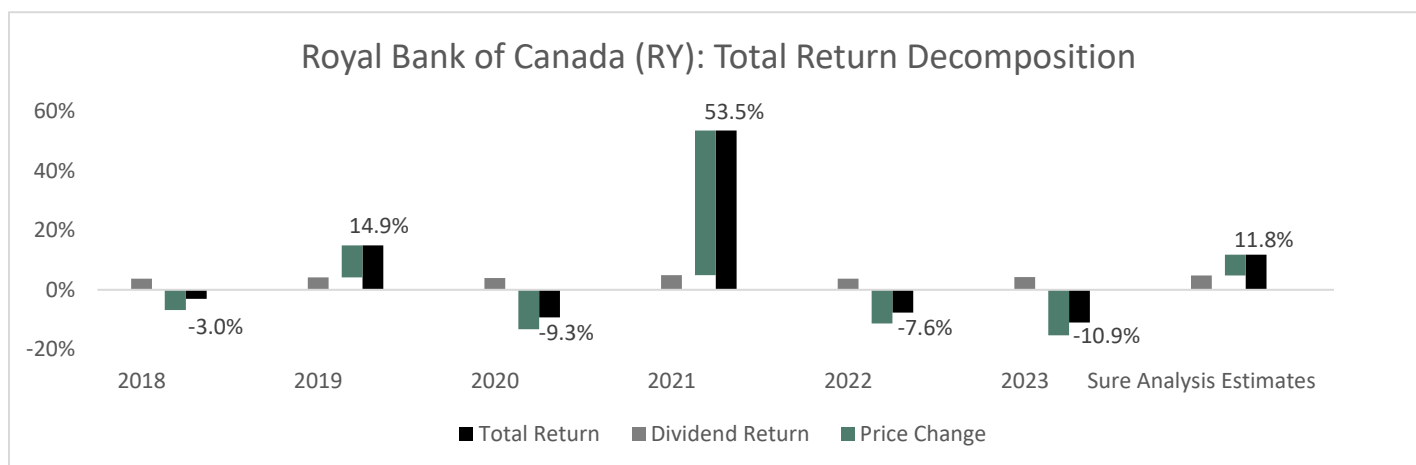
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	49%	49%	48%	45%	47%	46%	53%	40%	47%	47%	47%	47%

During the Great Recession in 2007-09, the stock increased its dividend every year (in the local currency of Canadian dollars), except for fiscal 2009 and 2010 in which it maintained the dividend. During that period, its adjusted EPS remained fairly stable and had a magnificent run from fiscal 2011 to 2019. The quality bank once again showed resilient earnings in fiscal 2020 in the midst of a pandemic. The regulator, Office of the Superintendent of Financial Institutions, once again stepped in to prevent the federally-rated Canadian banks to raise dividends during the pandemic. Investors were happy to know that the restriction was lifted in November 2021. RBC normally has a payout ratio of under 50%. The payout ratio was elevated a bit in fiscal 2020 but quickly came back down to below 50%. Competitive advantages are difficult to come by in banking, but RBC's franchise value, based on its history and scale, is a close substitute. We see RBC's brand as a valuable asset and one that should help it weather this and future economic downturns.

Final Thoughts & Recommendation

We rate RY as a Buy now. We forecast 11.8% in total returns annually over the next five years, consisting of a yield of 4.5%, 5.5% earnings-per-share growth, and a 2.6% tailwind from valuation expansion.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	31,150	28,280	28,710	30,680	33,040	34,440	35,040	39,370	37,880	41,690
SG&A Exp.	13,400	11,720	11,920	12,530	12,790	14,060	14,080	16,240	14,220	17,040
D&A Exp.	1,076	1,004	1,166	1,236	1,284	1,455	1,970	2,060	2,060	2,127
Net Profit	8,177	7,997	7,847	8,738	9,638	9,676	8,504	12,750	12,270	11,010
Net Margin	26.2%	28.3%	27.3%	28.5%	29.2%	28.1%	24.3%	32.4%	32.4%	26.4%
Free Cash Flow	12,800	18,380	19,310	27,800	12,040	9,030	101,310	46,780	15,100	17,300
Income Tax	2483	2093	2143	2449	2587	2290	2196	3641	3341	2668

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets (\$B)	839.9	816.1	879.8	945.4	1017.3	1085.2	1219.4	1376.9	1408.8	1450
Cash & Equiv. \$B)	23.1	26.7	31.9	47.6	50.8	49.1	118.5	156.1	132.6	96.2
Accounts Receivable	4,757	3,495	3,993	4,431	5,098	5,647	5,226	5,851	6,579	8,784
Goodwill & Int. Ass.	10200	9,190	11,780	12,070	12,060	12,080	12,050	12,370	13,490	13,380
Total Liabilities (\$B)	791.2	767.5	826.4	887.4	956.4	1021.7	1154.3	1297.2	1329.3	1365
Accounts Payable	5,530	4,300	4,280	4,680	6,620	6,330	7,100	8,480	12,700	14,900
Long-Term Debt	16783									
	3	182734	166623	177996	192070	206266	196599	242051	308660	314200
Shareholder's Equity	43411	43338	47932	52549	56061	59099	60587	74191	74023	79780
LTD/E Ratio	3.57	3.87	3.15	3.09	3.16	3.25	3.02	3.04	3.89	3.69

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	1.0%	1.0%	0.9%	1.0%	1.0%	0.9%	0.7%	1.0%	0.9%	0.8%
Return on Equity	19.4%	18.4%	17.2%	17.4%	17.7%	16.8%	14.2%	18.9%	16.6%	14.3%
ROIC	6.0%	3.6%	3.5%	3.8%	3.9%	3.7%	3.2%	4.4%	3.5%	2.8%
Shares Out.	1452	1450	1494	1474	1450	1441	1429	1427	1406	1393
Revenue/Share	21.46	19.51	19.21	20.81	22.78	23.9	24.52	27.6	26.94	29.94
FCF/Share	8.82	12.68	12.92	18.86	8.3	6.27	70.9	32.79	10.74	12.43

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

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