# Royal Bank of Canada (RY) Stock Pitch

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# Agenda

- Investment Recommendation
- Company Overview
- Investment Thesis
- Catalysts
- Valuation
- Risk Factors & Mitigation

# Investment Recommendation

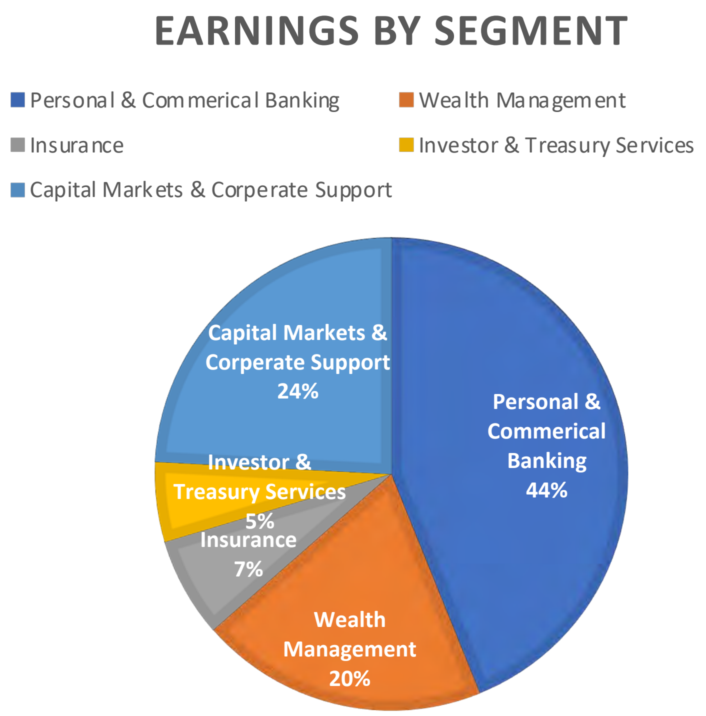
Buy RBC at a target price of 110 representing a ~10% upside.

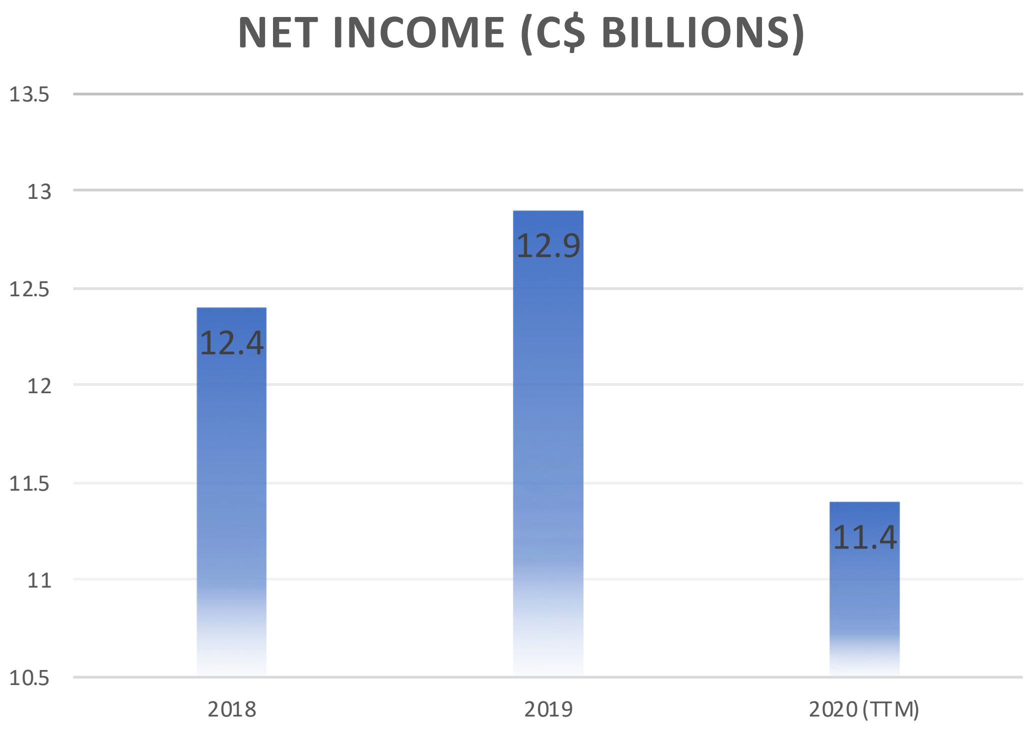
# Company Overview

# Royal Bank of Canada Overview

- Company Overview
  - History: Founded in 1864 as a private, unchartered bank for maritime merchants. Chartered upon Confederation in 1869, which resulted in rapid growth, seeing it rapidly grow to encompass all of Canada from coast to coast in only 18 years after being chartered, to eventually growing to be Canada’s largest bank.
  - Business Strategy: RBC’s primary business strategy is to be a broad & universal bank to continue to grow its already #1 spot in market share (in Canada).
  - Strategy (International): RBC is constructing a competitive business that primarily serves corporate/intuitional/high net worth clients that are attracted to the strong capabilities of RBC.

# Earnings Overview



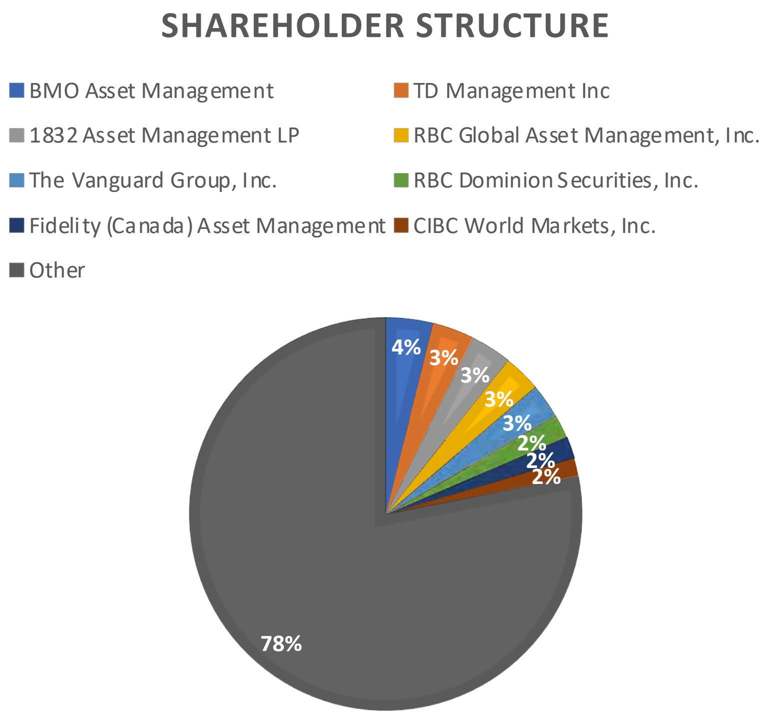



# Key Financials & Management Profiles

| | |
|---|---|
| Share Price | $101.71 |
| Market Cap | 132.492B |
| Dividend Yield | 4.3% |
| P/E Ratio | 12.91 |
| Revenue TTM | 36,089M |
| Profit Margin TTM | 23.49 |
| Debt-Equity | 0.13 |
| Historical Beta | 0.77 |
| Price to Book Ratio | 1.81 |
| ROE | 14.32% |

| | | |
|---|---|---|
| David McKay | CEO & President | Originally ran the Canadian Banking sector before being appointed, reinventing retail operations and introducing new technology. |
| Rod Bolger | CFO | Formerly served as the CFO for Bank of America & Citigroup before coming to RBC as the Executive VP of Finance. |
| Michael Dobbins | CSO | Was the Executive VP of RBC's largest banking segment, Personal Financing Products and led the aquation & merger of City National Bank, RBC's largest M&A. |

# Shareholder Structure




| Shareholder | % Owned |
|---|---|
| BMO Asset Management | 3.87% |
| TD Management Inc | 3.44% |
| 1832 Asset Management LP | 3.36% |
| RBC Global Asset Management, Inc. | 3.13% |
| The Vanguard Group, Inc. | 2.81% |
| RBC Dominion Securities, Inc. | 2.02% |
| Fidelity (Canada) Asset Management | 1.81% |
| CIBC World Markets, Inc. | 1.47% |

# Competition

- Toronto Dominion Bank
- Bank of Montreal
- Canadian Imperial Bank of Commerce
- Bank of Nova Scotia
- Desjardins, and other insurance firms
- Fidelity, and other investment houses

# Porter Analysis

Competitive Rivalry

- Despite being the largest chartered bank in Canada, RBC faces strong competition from the other big 4 banks, in particular TD, who is very close to RBC in market cap.

Threat of Substitutes

- As technology evolves, so does every industry, not even exempting banking & finance. The introduction of fintech appears to be revolutionizing the sector. But however, fintech or anything else is still too far to be a substitute for banking, meaning that RBC and other banks are fairy safe from a substitute other than themselves.

Threat of New Entrants

- The high capital requirements and legal hurdles of creating a chartered bank minimizes the amount of entrants into the industry and thus its risk.

# Porter Analysis (Cont.)

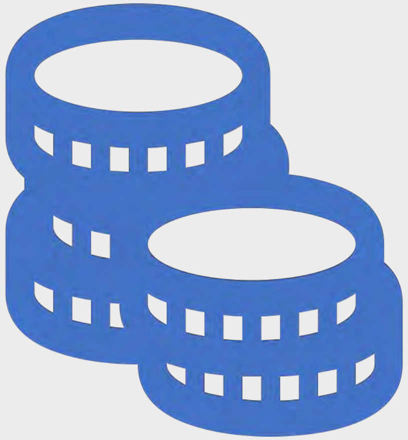
Bargaining Power of Buyers

- As there are 5 major banks in Canada to pick from, and each of them have a minimal risk of failure and an equally minimal difference in their services.  Canadians have the incentive to simply bank with whomever provides them the best deal, thus resulting in high bargaining power for buyers and a risk from it.

Bargaining Power of Suppliers

- The primary suppliers of a bank are customer deposits and other financial institutions.  As customers (buyers) have high bargaining power, and financial institutions  will obviously understand the importance of the supply of money to themselves, both customers and financial institutions have high bargaining power, thus increasing risk.

# Investment Thesis



# Why RY?

- Largest Market Capitalization in Canada
- Rock Solid Fundamentals
- Stability, Stability, and Stability

# Largest Market Capitalization in Canada

- RBC is the largest chartered bank across Canada, having a total market capitalization of 142.8 Billion
  - The next largest bank, TD has a market capitalization of 117 Billion
- RBC has a long history of utilizing its leading position in Canada to continue its growth and pursue its interests elsewhere
  - As such, RBC can have strong operations outside of Canada, in particular that in the US and the UK

# Rock Solid Fundamentals

- RBC has a return of equity of 13.51%, higher than that of the rest of the big four
- It sits at a conservative P/E ratio of 12.91 and historic of 12.47, signifying that the company is not overvalued
- At a Price to Book ratio of 1.81, RBC is lower than the vast majority of North American Banks, signaling undervaluation or at least relatively fair pricing
- Earnings have been growing steadily, reaching a record of 12.9 Billion in 2019

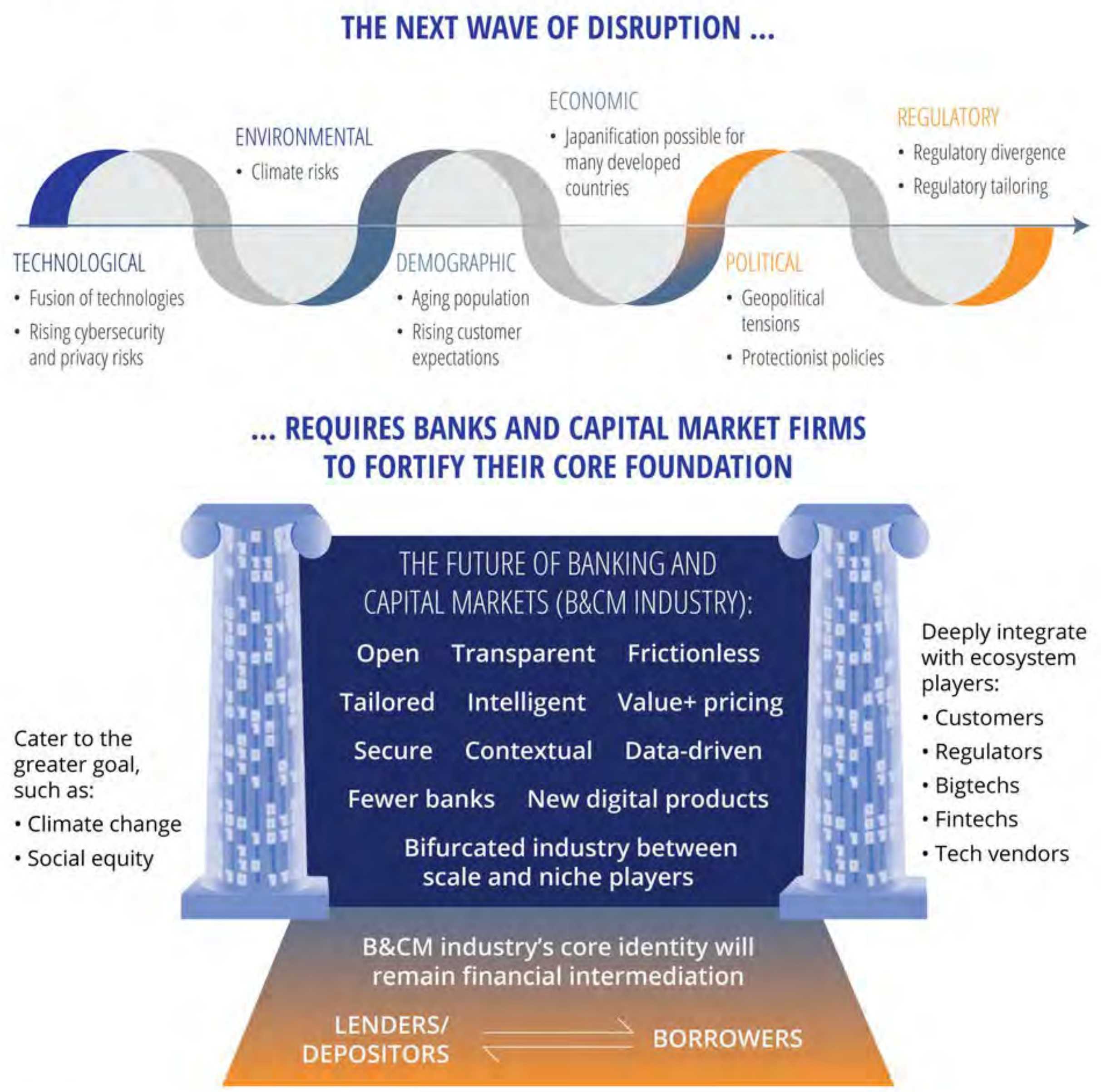
# Stability, Stability, and Stability

- RBC has not missed a dividend payment for 143 years
- Its dividend has been growing for the past decade, with a 26.41% increase over the past three years, all with a very conservative payout ratio of 49.45%
- The Canadian Banking sector is one of the most stable in the world, and should it fail we would have much larger problems than our stock portfolio
- Its historic beta of 0.74 ensures it is a safe choice in the market and an effective anchor for a portfolio

# Micro-Macro Outlook

FIGURE 1

**Fortifying the core for the next wave of disruption**




Source: Deloitte Center for Financial Services.

Deloitte Insights | deloitte.com/insights

# Disruption in the Banking Industry

# Sector Outlook

In the 2008 financial crisis, the banking sector emerged to be better capitalized, funded and liquid, with the capital basis of the largest banks doubling in the last decade, providing a light at the end of the tunnel regarding the current downturn.

- Governments have also been proven to consistently bail out institutions deemed to big to fail, thus limiting risk for the big banks.
- However, these downturns have commonly brought additional regulation to financial institutions.

The next wave of disruption of the banking sector is likely to be technological, but it is compounded with demographic and socioeconomic issues such as Japanification (persistent, slow economic growth), the impact of an aging population worldwide, and issues like climate change that will force banks to reprioritize (or at least appear to).

# Macroeconomic Concerns

The COVID-19 pandemic guarantees an oncoming recession & slowdown soon with unknown (but definitely high) severity.

- The likeliness of a V-shaped recovery is falling as the pandemic continues to rage on or return in the next wave.
    - However, recent vaccine developments may counteract this.
- Rising unemployment rates due to the pandemic will hurt spending and thus growth will fall, and unemployment will continue to rise, resulting in a vicious cycle. In addition, the question of what will happen when stimulus ends can only have a bad answer.
- This is important as the banking sector tends to move in the same direction as the economy, as it is the chief provider of liquidity.

# Catalyst & Risks

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## Catalysts

- Q4 earnings report
  - Analysts expect that sales growth is to decrease by -9.7% in the next quarter, giving a chance RBC might beat it.
  - Quarterly EPS is expected to increase to 2.44 from 2.22 (10% gain).
- The release of a COVID-19 vaccine, heralding economic recovery.

## Risks

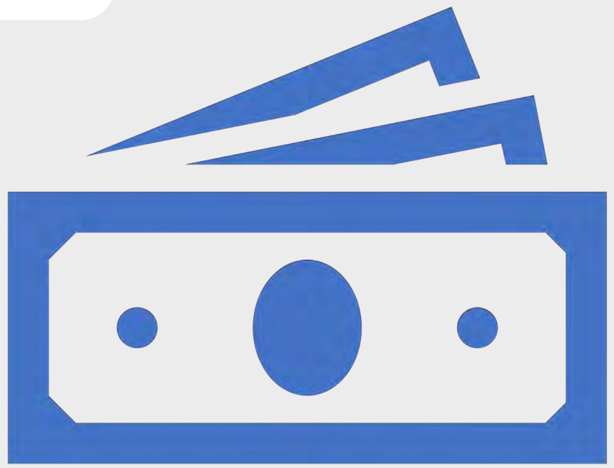
- Upcoming recession
  - Economic turbulence
  - Systemic market risk
- Competition

# Risk Mitigation

While the risk of investing in RBC is minimal, some steps can be taken to avoid some losses.

- If share prices continue to drop to to the overall market worsening from a COVID recession or other cause, RBC stock should be held as it is likely to recover along with the market.
- If RBC stock were to drop significantly more than the other major banks, it might be wise to liquidate as this would be unheard of.

# Valuation



# DCF Valuation

- Implied Value: $144
  - = 4.32/(7%-6.7%)
- 41.58% overvalued

| Current Price | 101.71 |
| --- | --- |
| Dividend Growth (5 Year Annualized) | 6.7% |
| WACC (Benchmark for large NA financial institutions) | 7% |
| Latest Dividend | 4.32 (Quarterly 1.08) |
| Expected Dividend Growth for the next period | 0% |

# DuPont Analysis

- As seen with the DuPont Analysis, RBC sits at the highest ROE with the largest Net Profit Margin and Asset Turnover, along with a high financial leverage ratio.

| Bank | Net Profit Margin | Asset Turnover | Financial Leverage | ROE |
|---|---|---|---|---|
| TD | 22.34% | 0.03 | 16.67 | 11.17% |
| Bank of Nova Scotia | 22.18% | 0.03 | 16.57 | 11.03% |
| Bank of Montreal | 17.74% | 0.03 | 23.51 | 12.51% |
| Canadian Imperial Bank of Commerce | 20.38% | 0.03 | 17.4 | 10.64% |
| **RBC** | **23.49%** | **0.03** | **20.32** | **14.32%** |

# Recommendations

- Buy RBC at a target price of 110 representing a ~10% upside.
- RBC stock is a safe choice that would follow a market recovery.

| Analyst Valuations (Yahoo Finance) | |
|---|---|
| **Rating** | **Target Price** |
| High | 127 |
| Low | 70 |
| Average | 105.17 |
| Average Rating | Buy (2.1) |

| Analysts | Target Price |
|---|---|
| National Bank Financial | 107 |
| TD Securities | 110 |
| Desjardins | 111 |
| Scotiabank | 105 |
| BMO Capital Markets | 97 |
| CIBC | 120 |