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While the best time to buy bank stocks has traditionally been autumn, the end of June makes a compelling case

Timing the sweet spot for Canadian banks


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Thackray's Investor's Guide, seasonal analyst Brooke Thackray's annual tome of investing recommendations, tells us that October is the time to buy the Canadian banks.

While the seasonal "sweet spot" for Canadian banks is usually later in the fall, there can also be a buying opportunity in the sector near the end of June. When the sector sells off into the broader market weakness that often occurs in June can be one of the more interesting times to consider the financials.

I usually look at the **BMO S&P/TSX Equal Weight Banks ETF** (ZEB-TSX, $26.95) when reviewing the banks. It's widely traded and is a fair representation of the bigger Canadian banks. The chart of ZEB on page 3 shows us that the upward trend for Canadian banks ended earlier this year. I correctly identified this trend change in March on my blog (www.valuetrend.ca).

Officially, there are no signs on the chart that the downward trend has ended. However, the near-termed view tells us that there may be an opportunity setting up. Let's take a look

The daily chart shows us a few encouraging signs – despite the fact that the major downtrend displayed by my trend lines has yet to be broken. Note the recent higher highs and lows on the near-termed chart.

Note the nice moves for money flow (see top and bottom panes). You can tell that investors are starting to become interested in the banks again, as evidenced by the rising momentum indicator MACD, and the RSI and stochastics indicators.

You can also see on the comparative relative strength line (the third pane from the bottom) that the banks are starting to outperform the TSX. This is interesting, given that the TSX is so focused on energy, materials and financials – and the banks themselves are so dependent on those other two sectors for their well-being. We're also seeing some volume picking up as the sector makes its first tepid steps towards a potential break of the larger declining trend.

Working against the banks are a potentially overvalued real estate market and rumblings from within the subprime sector after **Home Capital Group Inc.'s** (HCG-TSX, $18.67) recent problems.

New mortgage rules and the possibility of a slackening real estate market may result in slower growth for the sector. Something that continues to draw worry for the Bank of Canada is the rising consumer debt level of Canadian households. While the current ability to service this debt is not an issue, any shocks to the system might quickly change that. The banks have significant direct exposure to these high debt levels.

On the positive side of the ledger for Canadian banks are a few factors. First, several banks now generate significant revenue outside of Canada. The geographic diversification of their business goes a long way reducing Canada-specific risk.

Next, the energy exposure that many Canadian banks have is likely less impactful to earnings than in the past. Further, residential real estate mortgages by the big banks are not funded or exposed to the same criteria as alternative lenders.

Warren Buffett's Berkshire Hathaway has agreed to buy a 38 per cent share for $400 million and provide a $2 billion credit line to backstop Home Capital. Buffett's company has bailed out some of the biggest companies in the past.

Any impact Home Capital Group's problems have had on bank shares may just be an opportunity. Finally, we may, according to recent Bank of Canada commentary, be entering a period of less accommodative interest rates, which is traditionally positive for banks. Higher rates tend to generate greater profitability on their loans and mortgages.

The banks look interesting right now, although ideally I'd like to see a breakout of $27 per share for this ETF. That would prove a break from the declining trend and take out the last significant high on the daily chart. Alternatively, investors happy with the dividends could instead buy them and wait that potential occurrence to play out.

Keith on BNN

Keith will be on BNN's popular call-in show Market Call on Monday, July 24 at 5:30 p.m. Phone in with your questions on technical analysis for Keith during the show. Call toll-free at 1-855-326-6266, or email your questions ahead of time (specify they are for Keith) to marketcall@bnn.ca.

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