

Bank of Nova Scotia

Long Road to Recovery

Reiterate Rating: NEUTRAL | PO: 68.00 CAD | Price: 64.52 CAD

Stock bounce reflects weak sentiment, lower yields

Scotia (BNS) shares outperformed peers after reporting a relatively uneventful quarter (Exhibit 1). We attribute the outperformance to the weak investor sentiment that has led to a relatively discounted valuation (1.1x P/B, ~6.5% div. yield) and the fact that bond yields dropped sharply on softer macro-economic data. Revise FY24e EPS to \$7.10 from \$7.38 with the negative EPS revision driven by a lower revenue growth outlook. Our EPS forecast implies a relatively elevated dividend payout ratio of 60% for both FY23/FY24.

Strong capital build

The common equity tier 1 (CET1) capital ratio rose to 12.7% (+38bps QoQ) with expectations for this ratio to move towards 13% by YE23. This positions the bank well to absorb the negative impact from the adoption of new market risk (FRTB) rules and Basel floor factor increase – both in 1Q24. Moreover, Scotia should also be well positioned to handle another potential increase in the domestic stability buffer (DSB) that would push minimum CET1 requirement to 12% from the current 11.5%.

Mixed bag in LatAm

International banking segment (contributes 35% to total revenues; includes LatAm) witnessed continued credit normalization with PCLs +15bp QoQ to 1.18% vs. 1.36% reported for 4Q19. The increase was driven by Peru (+72bp) and Chile (+43bp) that is already in a recession. Mexico remains a bright spot (lift from near shoring) and we expect the country to become the centerpiece of Scotia's LatAm retail/commercial banking strategy. BofA Economics team forecasts GDP growth across LatAm to slightly moderate to +1.6% in FY24 vs. +1.8% in FY23. Relevant Research: "LatAm At A Glance".

Franchise turnaround a multi-year story

While new leadership appears to be on the right track, we note that the benefit of mgmt's actions (emphasis on deposits, primacy of client relationships, profitability over growth) are unlikely to move the needle on growth/ROE anytime soon (assuming seamless execution). We think the stock will need some macro help, specifically rate-cuts, to get investors excited about the earnings outlook, while they wait for strategic actions to take hold. We roll forward our PO methodology to 2024 P/E (50% weight) and P/YE24e book value (50%). Reiterate Neutral and lower PO to \$68 from \$70.

Estimates (Oct) (C\$)	2021A	2022A	2023E	2024E	2025E
EPS	7.88	8.49	7.02	7.10	7.80
GAAP EPS	7.71	8.01	6.49	7.05	7.76
EPS Change (YoY)	47.3%	7.7%	-17.3%	1.1%	9.9%
Consensus EPS (Bloomberg)			7.10	7.41	7.85
DPS	3.60	4.06	4.18	4.26	4.30
EPS (BNS - US\$)	6.26	6.59	5.16	5.22	5.74
DPS (BNS - US\$)	2.86	3.15	3.07	3.13	3.16
Valuation (Oct)					
P/E	8.2x	7.6x	9.2x	9.1x	8.3x
GAAP P/E	8.4x	8.1x	9.9x	9.2x	8.3x
Dividend Yield	5.6%	6.3%	6.5%	6.6%	6.7%

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Timestamp: 29 August 2023 09:15PM EDT

29 August 2023

Equity

Key Changes

(C\$)	Previous	Current
Price Obj.	70.00	68.00
2023E Rev (m)	32,170.1	32,109.6
2024E Rev (m)	33,899.6	33,310.0
2025E Rev (m)	35,926.6	35,803.4
2023E EPS	7.15	7.02
2024E EPS	7.38	7.10
2025E EPS	7.86	7.80
2023E DPS	4.21	4.18

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Stock Data

Price (TOR / NYS)	64.52 CAD / 47.58 USD
Price Objective	68.00 CAD / 52.00 USD
Date Established	29-Aug-2023 / 28-Feb-2023
Investment Opinion	A-2-7 / B-2-7
52-Week Range	61.46 CAD - 74.78 CAD
Market Value (mn)	77,307 CAD
Average Daily Value (mn)	230.83 USD
Shares Outstanding (mn)	1,198.2 / 1,198.2
BofA Ticker / Exchange	YBNS / TOR
BofA Ticker / Exchange	BNS / NYS
Bloomberg / Reuters	BNS CN / BNS.TO
ROE (2023E)	12.6%
ESGMeter™	High

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to "BofA ESGMeter Methodology".

iQprofileSM Bank of Nova Scotia

Income Statement Data (Oct)

(C\$ Millions)	2021A	2022A	2023E	2024E	2025E
Net Interest Income	16,961	18,115	18,176	18,719	20,403
% change	-2.1%	6.8%	0.3%	3.0%	9.0%
Net Fee Income	NA	NA	NA	NA	NA
Securities Gains / (Losses)	NA	NA	NA	NA	NA
Total Operating Income	31,252	31,777	32,110	33,310	35,803
Operating Expenses	(16,430)	(16,884)	(18,120)	(18,553)	(19,434)
% change	-1.4%	2.8%	7.3%	2.4%	4.8%
Provisions Expense	(1,808)	(1,382)	(3,038)	(3,715)	(3,996)
% change	-69.5%	-23.6%	119.8%	22.3%	7.6%
Operating Pre-Tax Income	13,433	13,585	11,082	11,042	12,373
Operating Net Income to Comm S/Hold.	9,666	10,265	8,494	8,658	9,511
GAAP Net Income	9,457	9,680	7,852	8,598	9,454

Balance Sheet Data (Oct)

(C\$ Millions)	2021A	2022A	2023E	2024E	2025E
Total Assets	1,184,844	1,349,418	1,401,041	1,457,000	1,508,510
Average Interest Earning Assets	NA	NA	NA	NA	NA
Total Gross Customer Loans	642,612	750,335	760,509	780,026	816,543
% change	5.2%	16.8%	1.4%	2.6%	4.7%
Total Customer Deposits	797,259	916,181	970,799	1,013,086	1,051,593
% change	6.2%	14.9%	6.0%	4.4%	3.8%
Tangible Equity	48,146	48,317	51,871	55,336	59,605
Common Shareholders' Equity	72,892	74,749	78,855	82,260	86,472

Key Metrics (Oct)

(C\$ Millions)	2021A	2022A	2023E	2024E	2025E
Net Interest Margin	NA	NA	NA	NA	NA
Effective Tax Rate	21.7%	20.9%	18.1%	17.8%	19.7%
Loan / Deposit Ratio	80.6%	81.9%	78.3%	77.0%	77.6%
Tangible Common Equity / Assets	4.1%	3.6%	3.7%	3.8%	4.0%
ROA	0.84%	0.80%	0.61%	0.60%	0.63%
ROE	15.1%	15.7%	12.6%	12.2%	12.7%
RoTE	20.6%	21.3%	17.0%	16.1%	16.5%
Dividend Payout Ratio	45.7%	47.8%	59.5%	60.0%	55.1%
Efficiency Ratio (Cost / Income Ratio)	52.6%	53.1%	56.4%	55.7%	54.3%

Quality of Earnings (Oct)

(C\$ Millions)	2021A	2022A	2023E	2024E	2025E
Total Non-Interest Inc / Operating Inc	45.7%	43.0%	43.4%	43.8%	43.0%
NPLs plus Foreclosed Real Estate / Loans	0%	0%	0%	0%	0%
Loan Loss Reserves / NPLs	NA	NA	NA	NA	NA
Loan Loss Reserves / Total Loans	0%	0%	0%	0%	0%

Company Sector

Banks-Multinational/Universal

Company Description

Scotiabank is the third-largest Canadian bank by market capitalization, and is the most international of the Canadian banks. In recent years, the bank has begun to consolidate operations, focusing more on Latin American countries, primarily Peru, Mexico, Chile, and Colombia, and less on Asia and the Caribbean.

Investment Rationale

While the stock screens attractively, trading at a discounted valuation and offering an above peer average dividend yield, limited idiosyncratic catalysts combined with an increasingly uncertain macro backdrop keep us at a Neutral recommendation.

Stock Data

Average Daily Volume	4,865,698
Shares / Common - Dual Listed	1.00

Quarterly Earnings Estimates

	2022	2023
Q1	2.15A	1.85A
Q2	2.18A	1.70A
Q3	2.10A	1.73A
Q4	2.06A	1.74E

Key Changes

(US\$)	Previous	Current
2023E EPS	5.26	5.16
2024E EPS	5.43	5.22
2025E EPS	5.78	5.74
2023E DPS	3.10	3.07

Exhibit 1: BNS 3Q23 earnings variance table

Earnings results vs. BofA and consensus estimates

BNS 3Q23 (C\$m)	Actual	Cons	vs. Cons	BofAe	vs BofAe
Consolidated					
Net Income	2,103	2,088	0.7%	2,098	0.2%
Revenue	8,090	8,166	-0.9%	8,027	0.8%
Expense	4,542	4,539	0.1%	4,547	-0.1%
PTPP	3,548	3,622	-2.0%	3,480	1.9%
PCLs	819	773	6.0%	758	8.0%
Net Interest Income	4,580	4,747	-3.5%	4,608	-0.6%
Tax Rate	18.4%	23.3%	-490bp	18.3%	10bp
Issuance/(Buybacks) (mn shares)	7.2	5.3	37.0%	0.0	-
Adj. EPS	1.73	1.74	-0.6%	1.75	-1.3%
Canadian Banking					
Net Income	1,063	1,100	-3.4%	1,101	-3.4%
Revenue	3,216	3,097	3.8%	3,278	-1.9%
Expense	1,447	1,470	-1.6%	1,492	-3.0%
PTPP	1,769	1,627	8.8%	1,787	-1.0%
PCLs	307	269	14.1%	272	13.0%
Net Interest Income	2,468	2,427	1.7%	2,483	-0.6%
Loan Growth (QoQ)	-0.1%	0.8%	-90bp	1.3%	-140bp
NIM	2.35%	-		2.33%	2bp
International Banking					
Net Income	635	678	-6.3%	697	-8.9%
Revenue	2,846	2,751	3.4%	2,852	-0.2%
Expense	1,481	1,535	-3.5%	1,483	-0.1%
PTPP	1,365	1,217	12.2%	1,369	-0.3%
PCLs	516	479	7.8%	451	14.5%
Net Interest Income	2,118	2,114	0.2%	2,088	1.4%
Loan Growth (QoQ)	0.5%	1.8%	-130bp	1.8%	-130bp
NIM	4.10%	-		4.12%	-2bp
Global Wealth					
Net Income	373	392	-4.8%	375	-0.5%
Revenue	1,336	1,350	-1.0%	1,328	0.6%
Expense	834	842	-0.9%	817	2.1%
PTPP	502	508	-1.2%	511	-1.8%
PCLs	2	2	7.2%	2	0.0%
Global Banking					
Net Income	434	412	5.3%	370	17.2%
Revenue	1,343	1,219	10.2%	1,225	9.6%
Expense	758	664	14.1%	686	10.5%
PTPP	585	555	5.4%	539	8.5%
PCLs	(6)	26	-122.7%	34	-117.7%
Corp					
Net Income	(299)	(372)	-19.6%	(345)	-13.4%
Revenue	(651)	(578)	12.6%	(656)	-0.8%
Expense	22	37	-40.8%	69	-68.3%
PTPP	(673)	(615)	9.4%	(726)	-7.3%
PCLs	0	0	-	0	-

Source: BofA Global Research estimates, VisibleAlpha, company filings

BofA GLOBAL RESEARCH

Price objective basis & risk

Bank of Nova Scotia (YBNS / BNS)

Our \$68 PO (US\$52) is calculated based off of applying a P/BV multiple of 1.2x (50% weight) to our YE24e BV and a 9.0x P/E (50% weight) to our 2024eP/E. These multiples are in-line with peer multiples at 9.5x P/E and 1.2 P/B for the group.

Upside risks: 1) continued resilience of the Canadian consumer and thereby its housing market could alleviate the risk from a housing slowdown, 2) better than expected economic growth in the LatAm markets, which could accelerate loan growth and keep credit losses at a moderate level, and 3) successful push to grow core deposits and thereby improve profitability through a shift in funding mix toward lower-cost source of funds.

Downside risks: 1) a sharp downturn in the Canadian housing market and rise in unemployment rate could lead to higher credit losses, 2) a worse than expected slowdown in Latin American economies could lead to anemic loan growth and accelerating credit losses, 3) inability to grow core deposits and continued reliance on higher cost of funds, thereby weakening profitability.

Analyst Certification

I, Ebrahim H. Poonawala, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North America - Banks Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Citigroup Inc.	C	C US	Ebrahim H. Poonawala
	Cullen/Frost Bankers Inc	CFR	CFR US	Ebrahim H. Poonawala
	East West Bancorp, Incorporated	EWBC	EWBC US	Ebrahim H. Poonawala
	Fifth Third Bank	FITB	FITB US	Ebrahim H. Poonawala
	First Bancorp Puerto Rico	FBP	FBP US	Brandon Berman
	First Horizon Corporation	FHN	FHN US	Ebrahim H. Poonawala
	Goldman Sachs	GS	GS US	Ebrahim H. Poonawala
	JPMorgan Chase & Co.	JPM	JPM US	Ebrahim H. Poonawala
	KeyCorp	KEY	KEY US	Ebrahim H. Poonawala
	M&T Bank	MTB	MTB US	Ebrahim H. Poonawala
	Morgan Stanley	MS	MS US	Ebrahim H. Poonawala
	New York Community Bancorp	NYCB	NYCB US	Ebrahim H. Poonawala
	Synovus Financial Corp.	SNV	SNV US	Ebrahim H. Poonawala
	The Bank of New York Mellon Corporation	BK	BK US	Ebrahim H. Poonawala
	Toronto-Dominion Bank	TD	TD US	Ebrahim H. Poonawala
	Toronto-Dominion Bank	YTD	TD CN	Ebrahim H. Poonawala
	U.S. Bancorp	USB	USB US	Ebrahim H. Poonawala
	Wells Fargo & Company	WFC	WFC US	Ebrahim H. Poonawala
	Western Alliance Bancorp	WAL	WAL US	Ebrahim H. Poonawala
NEUTRAL				
	Ally Financial	ALLY	ALLY US	Brandon Berman
	Associated Banc-Corp	ASB	ASB US	Brandon Berman
	Bank of Montreal	BMO	BMO US	Ebrahim H. Poonawala
	Bank of Montreal	YBMO	BMO CN	Ebrahim H. Poonawala
	Bank of Nova Scotia	YBNS	BNS CN	Ebrahim H. Poonawala
	Bank of Nova Scotia	BNS	BNS US	Ebrahim H. Poonawala
	Citizens Financial Group	CFG	CFG US	Ebrahim H. Poonawala
	Comerica Incorporated	CMA	CMA US	Ebrahim H. Poonawala
	Huntington Bancshares Inc.	HBAN	HBAN US	Ebrahim H. Poonawala
	Regions Financial	RF	RF US	Ebrahim H. Poonawala
	Royal Bank of Canada	RY	RY US	Ebrahim H. Poonawala

North America - Banks Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Royal Bank of Canada	YRY	RY CN	Ebrahim H. Poonawala
	State Street Corporation	STT	STT US	Ebrahim H. Poonawala
	Truist Financial	TFC	TFC US	Ebrahim H. Poonawala

UNDERPERFORM

	Bank of Hawaii Corp.	BOH	BOH US	Brandon Berman
	Canadian Imperial Bank of Commerce	CM	CM US	Ebrahim H. Poonawala
	Canadian Imperial Bank of Commerce	YCM	CM CN	Ebrahim H. Poonawala
	First Hawaiian Inc.	FHB	FHB US	Brandon Berman
	Prosperity Bancshares Inc.	PB	PB US	Ebrahim H. Poonawala
	Texas Capital Bancshares Inc.	TCBI	TCBI US	Brandon Berman
	The PNC Financial Services Group, Inc.	PNC	PNC US	Ebrahim H. Poonawala
	Zions Bancorp	ZION	ZION US	Ebrahim H. Poonawala

IQmethodSM Measures Definitions**Business Performance**

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization

Shareholders' Equity

Sales

N/A

N/A

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

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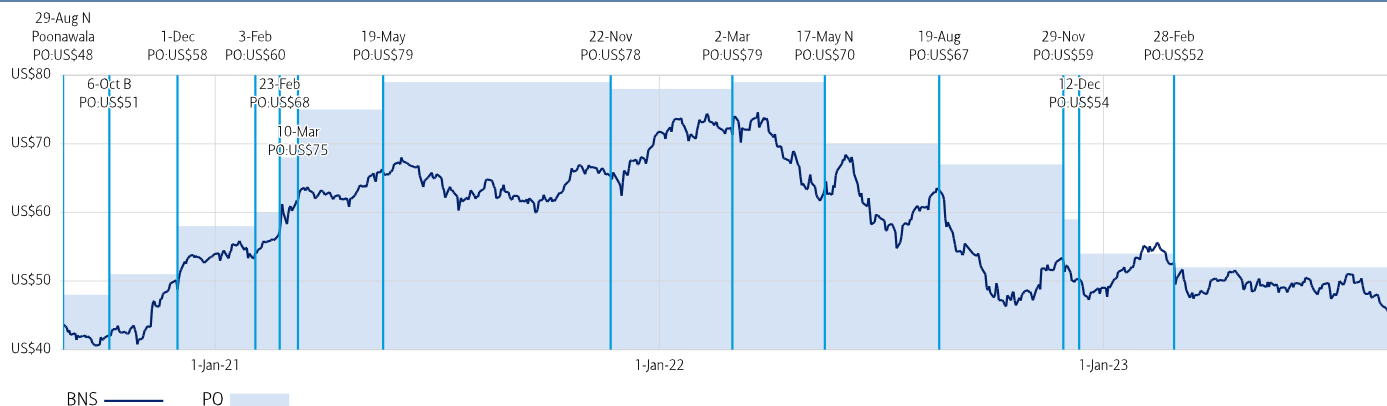
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Important Disclosures

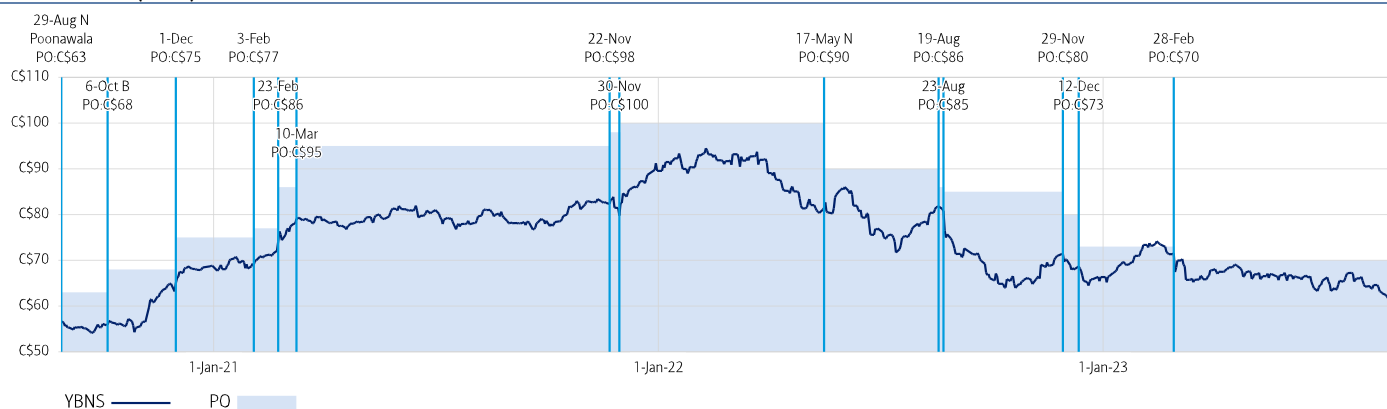
Bank of Nova Scotia (BNS) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Bank of Nova Scotia (YBNS) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Banks Group (as of 30 Jun 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	98	50.52%	Buy	81	82.65%
Hold	45	23.20%	Hold	33	73.33%
Sell	51	26.29%	Sell	37	72.55%

Equity Investment Rating Distribution: Global Group (as of 30 Jun 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1877	53.28%	Buy	1040	55.41%
Hold	815	23.13%	Hold	464	56.93%
Sell	831	23.59%	Sell	385	46.33%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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