



How Expensive Are Canadian Stocks? A Look at the S&P/TSX Composite Index

Description

The **S&P/TSX Composite Index** (TSX: ^OSPTX) is up about 2% year to date, after posting a 4% gain in 2012.

The S&P/TSX held up better than the **Dow Jones Industrial Average** (INDEX: ^DJI) during the financial crisis of 2008, so its recovery since 2009 hasn't been as massive, and it's still below its all-time high. (The Dow broke its all-time record back in March.) Still the two indices have roughly mirrored each other over the past 10 years:

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Source: Google Finance. Blue line = S&P/TSX Composite. Red = Dow Jones Industrial Average.

The S&P/TSX Composite covers about 70% of the market capitalization of Canadian stocks, and so is a fair representation of the overall market. With that in mind, let's look at its current valuation, relative to the past four calendar years:

S&P/TSX Composite Index	Current	2012	2011	2010	2009
P/E	19.1	18.0	16.8	17.9	30.6
P/B	1.8	1.8	2.0	2.2	2.3
ROE	9.3%	10.1%	12.0%	12.1%	8.1%
Net Income Margin	8.2%	8.8%	9.9%	10.2%	6.7%

Data from S&P Capital IQ.

The price-to-earnings ratio of Canadian stocks has inched up in the past few years, even as price-to-book multiples have decreased slightly. At the same time, returns on equity and net income margin figures have bounced around.

Compared with the Dow, the Canadian figures look less enticing. Even as the Dow has reached new highs, its P/E and P/B multiples have come down, while its ROE and net income margin have edged slightly higher:

Dow Jones Industrial Average	Current	2012	2011	2010	2009
P/E	16.5	16.7	16.8	17.6	22.2
P/B	2.4	2.5	2.6	2.6	2.8
ROE	15.4%	15.4%	16.2%	15.9%	14.6%
Net Income Margin	9.6%	9.3%	9.6%	9.9%	9.1%

Data from S&P Capital IQ.

Not only are Canadian stocks more expensive relative to their American neighbours, the S&P/TSX Composite is flawed for index-tracking — it's overweight in resource and financial stocks, meaning index investors lack proper diversification.

We have created an exclusive free report detailing "[5 Stocks That Should Replace Your Canadian Index Fund](#)," designed as an easy-to-implement strategy for market-beating returns. To download a copy of this FREE report, simply [click here right now](#).

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This post was created by Fool contributor Brian Richards.

Fool contributor Brian Richards does not own shares of any of the companies mentioned at this time. The Motley Fool has no positions in the stocks mentioned above.

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