

The Bull Case for TD Bank

Description

We're a motley bunch here at Motley Fool Canada and often disagree about a stock's prospects. My fellow Fool Benjamin Sinclair's article "[3 Reasons Not to Buy TD Bank](#)" caused me to reevaluate my own bullish thesis on the stock.

Benjamin's thesis is that investors are paying a premium for a company that is struggling to grow internationally and faces significant risks here at home. There is merit to this argument and there are certainly some smart investors who agree. However, I think there's a bullish case to be made for **TD Bank** ([TSX: TD](#))([NYSE: TD](#)). Here's why.

1. U.S. expansion is the right strategy

TD's focus on the U.S., where it actually has more branches than it does in Canada, has concerned many investors. Return on equity for the U.S. operations is under 10%, compared to over 40% in Canada.

As I have discussed previously ([here](#), [here](#), and [here](#)), I'm not a fan of companies that grow just for the sake of growth. If a business cannot generate a sufficient return for shareholders in their new ventures, management should always return capital back to investors in the form of dividends and buybacks.

However, TD doesn't fit into this category. Thanks to the company's huge size and prudent management, the firm has a low cost of capital. So even if TD cannot generate Canadian-like returns from its U.S. operations, double-digit returns are more than sufficient for shareholders.

2. Canadian slow down is already priced in

No doubt, a Canadian slow down would negatively impact TD. In a worst-case scenario, would put a large part of the banking industry's tangible equity at risk. However, it's domestic banks like the **National Bank of Canada** ([TSX: NA](#)) and the **Canadian Imperial Bank of Commerce** ([TSX: CM](#))([NYSE: CM](#)) that are the most at risk. Institutions with a larger international presence would be less affected. Institutions with the most international exposure like **Royal Bank** ([TSX: RY](#))([NYSE: RY](#)) and TD would have the least exposure.

In addition, concerns of a Canadian real estate bubble have been discussed for years. In every single conference call, TD's CEO Ed Clark has discussed these risks. The company has had ample time mitigate the consequences of housing bust.

3. Pay up for best of breed

Yes, TD is the most expensive of the top Canadian banks. But I believe that when it comes to valuation multiples, investing in the more expensive stock is usually worth it for the peace of mind. It's a bit like buying a \$9 pair of jeans at

Walmart versus a \$79 pair at **The Bay**. Sometimes you get what you pay for.

Now whether 14 times earnings is a fair price to pay for TD is a little beyond the scope of this article. However, the company is growing earnings and dividends faster than any of its peers, which would justify the premium valuation at first glance. Dismissing the stock because of its richer price tag is mistaken.

Foolish bottom line

We Fools may not always hold the same views, but considering a wide range of insights and opinions makes us better investors. TD Bank certainly faces some headwinds. However, I believe management is pursuing the correct strategy. And given that the stock is growing faster than its peers, it's worth paying a premium for.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:TD (The Toronto-Dominion Bank)
2. TSX:CM (Canadian Imperial Bank of Commerce)
3. TSX:NA (National Bank of Canada)
4. TSX:RY (Royal Bank of Canada)
5. TSX:TD (The Toronto-Dominion Bank)

Category

1. Investing

Date

2025/07/06

Date Created

2014/03/31

Author

rbaillieul

default watermark