The Best Way to Bet on U.S. Banking

Description

It's no secret that banking in the United States is a tough business. With nearly 7,000 total banks in the country, competition is fierce, and profitability is difficult to come by. Making matters worse, not enough businesses nor consumers want to borrow money, meaning banks are struggling to invest the money available to them. And that's an uphill battle thanks to stubbornly low interest rates.

But there are reasons for optimism. With housing still fairly depressed, there is still more upside than downside in the real estate market. The same thing could be said for interest rates. And thanks to regulatory reforms, big banks are better capitalized and more disciplined than before the crisis.

So what's the best way to bet on the sector? The Canadian banks in the United States, or the U.S. banks themselves? Below we take a look at each option.

Canadian banks in America

Both **TD Bank** (TSX: TD)(NYSE: TD) and **Bank of Montreal** (TSX: BMO)(NYSE: BMO) have extensive banking operations in the United States, with TD Bank focusing on the east coast and Bank of Montreal on the midwest.

It hasn't been easy for either of them. In 2013, TD Bank reported a return on equity of 8.1% for its U.S. banking division, compared to 46.8% for Canadian banking. Other measures tell a similar story. Net income per employee in the United States was just over $60,000, compared to nearly $130,000 in Canada.

The story was fairly similar for Bank of Montreal; although the bank doesn't disclose returns on equity by geography, it was certainly more profitable in Canada than in the United States. Net income per employee in the U.S. banking division was $73,000, compared to $116,000 in Canada.

If you're looking to bet on U.S. banking through one of the Canadian banks, then TD Bank is likely the better option. Its U.S. banking division accounted for 23% of its total income, while that number was only 14% at Bank of Montreal. It will also likely be growing its U.S. banking operations more than Bank of Montreal in the coming years. And finally, it has a better Canadian banking franchise than Bank of

Montreal, as well as a better track record.

American banks

But there is a better alternative: Invest in one of the large American banks. One that stands out is **Bank of America** (NYSE: BAC). The bank has certainly had its share of turbulence in recent years, including hefty fines and a capital calculation error. But the shares are incredibly cheap, trading at 0.7 times book value.

For those of you looking for a higher-quality bank, look no further than **Wells Fargo** (NYSE: WFC), which is 9.2% owned by Warren Buffett's **Berkshire Hathaway** (NYSE: BRK-A). Although the shares are more expensive at 1.7 times book value, the company has a return on equity of 14%, easily beating TD Bank.

Either of these companies offer plenty of upside for the risk you'd be taking. As a bonus, you don't have to worry about Canadian real estate with these picks.

CATEGORY

1. Investing

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1. NYSE:BAC (Bank of America)
2. NYSE:BMO (Bank of Montreal)
3. NYSE:TD (The Toronto-Dominion Bank)
4. NYSE:WFC (Wells Fargo)
5. TSX:BMO (Bank Of Montreal)
6. TSX:TD (The Toronto-Dominion Bank)

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