Key Things to Watch in Toronto-Dominion Bank's Upcoming Report

Description

Toronto-Dominion Bank (TSX: TD)(NYSE: TD) is the sixth largest bank in North America by branches and counts 22 million customer as clients. The Canadian Retail Banking operation currently makes the largest contribution to net income at 65% followed by 27% from the U.S. Retail Banking and 11% from the Wholesale Banking operations.

Second-quarter profit was higher than expected

Second-quarter 2014 financial results were better than expected with adjusted earnings per share 15% ahead of the previous year. The overall business performed well with all divisions except Wholesale Banking reporting improved results. The star performance came from the U.S. Retail Banking division, supported by the weaker Canadian dollar. The return on equity of the overall business, a key measure of performance, also improved slightly to 16.6% during the quarter.

Further all-round improvement expected for the third quarter

The bank is expected to report results on August 28 and consensus expectations at the earnings per share level for the third quarter are set at $1.10, which will represent an increase of 33% compared to the previous year. The third quarter of 2013 was the weakest of the 2013 financial year, caused by losses in the insurance business resulting from increased weather-related and general insurance claims. The base for comparison will therefore be relatively low.

Toronto-Dominion is on record stating that the objective is to grow earnings per share by 7%-10% for the full year and seems to be on track to exceed this target.

The Canada Retail division should deliver strong results

The Canadian Retail banking division, which includes personal and commercial banking, insurance, and wealth management, is the largest and most profitable contributor to profits. Overall lending and deposit growth is expected to remain slow in Canada but the quarter could turn out to be very good for this division as the benefits of the $3.3 billion acquisition of the 540,000 Aeroplan credit cardholder portfolio at the end of 2013 will start to show up in the results. The third-quarter losses experienced last year by the Insurance division are not expected to be repeated giving further impetus to the results of the Canadian retail unit.

The U.S. Retail division has an operating performance profile substantially inferior to the Canadian Retail operation. This was discussed in more detail in my recent article but in short, the return on equity of the U.S. operation is about 20% of the profitability level of the Canadian operation, cost efficiency is 33% worse and provision for credit losses is double. Although there are signs of improvement, considerable improvement is still possible.

Also part of U.S. Retail business is the investment in the stockbroker **TD Ameritrade Holding Corp** (NYSE: AMTD). This company has been performing well on the back of strong improvements in the financial markets – the bank has already announced that the contribution of TD Ameritrade to the third-quarter results should be $76 million – which is a little more than last year despite the fact that the bank sold about 10% of its shares in Ameritrade since last year.

The smaller Wholesale Banking division includes capital markets services and corporate lending. Profit in this division is somewhat unpredictable as a result of the influence of trading and merger and acquisition advisory services. Apart from the revenue generating activities, the high cost levels will be scrutinised for improvement in the third quarter.

The share price has been performing well

The share price has been doing well over the past year adding 32% plus a dividend of around 3.5% and outperforming the other major Canadian banks. The share is still not expensively valued at a 12-month forward price-to-earnings ratio of 12.4 times, a dividend yield of 3.5% and with profit growth seemingly moving along at an accelerating pace, could continue to do well.

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