2 Reasons to Avoid Toronto-Dominion Bank, and 1 Stock to Buy Instead

Description

If you're building a portfolio of Canadian stocks, the banks are a great place to start. They face limited competition, generate plenty of profits, and are very safe by international standards. It's no wonder that so many professionally managed funds have a Canadian bank as the largest holding.

To be more specific, **Toronto-Dominion Bank** (TSX: TD)(NYSE: TD) is a particularly popular stock to hold, and again this should be no surprise. TD is a best-in-class bank, with a great track record. And its shares have done very well recently, up 50% in the last three years.

But there are reasons not to go with TD. Below we take a look at two of them, as well as a different Canadian bank to buy instead.

Reasons to avoid TD

1. The United States of America

In Canada, TD seemingly can do no wrong. It competes for leading market share in most products, wins awards for customer satisfaction, and makes over 40% return on equity. The United States has been a different story.

TD first entered the USA 10 years ago, and it has been a struggle. The financial crisis did not help, especially since TD made a big acquisition right before the crisis began. Even after the crisis ended, the recovery has been slow and interest rates have remained depressed, both of which have held TD back. But the real problem is the intense competition, which ensures that profit margins stay very thin.

Unfortunately, the USA is where TD has the most room to grow. The bank is determined to increase its footprint south of the border, and that should help the bottom line. But as an investor, you rarely want to see any company grow in one of its lowest-return lines of business.

2. Price

As mentioned above, TD shares have done very well. But that comes with a problem. At over 14 times earnings, TD is the most expensive of Canada's big five banks. And as a result, it also has the lowest dividend yield, at just over 3%. TD also trades at over two times book value.

By comparison, many of the biggest American banks trade at less than one times book value. So if you're looking to make a bet on the USA specifically, that's probably the better option.

1 stock to buy instead: Bank of Nova Scotia

While TD is focusing on the United States, it's a much different story at **The Bank of Nova Scotia** (TSX: BNS)(NYSE: BNS), which focuses primarily on emerging markets. More specifically, the bank is emphasizing Mexico, Colombia, Peru, and Chile.

These countries have much more potential than the United States. Their economies are growing more quickly, the population is generally under-banked, and competition is less intense. So all of these factors should help Bank of Nova Scotia grow and thrive outside of Canada.

Remarkably, Bank of Nova Scotia trades at just 12.3 times earnings, making it the cheapest out of the big 5. Clearly the bank is not as popular as TD. But at this point, it seems to be the better option.

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