Royal Bank of Canada, Toronto-Dominion Bank, or The Bank of Nova Scotia: Which Should You Choose?

Description

Royal Bank of Canada (TSX: RY)(NYSE: RY), **Toronto-Dominion Bank** (TSX: TD)(NYSE: TD), and **The Bank of Nova Scotia** (TSX: BNS)(NYSE: BNS) are not only Canada's three largest banks but are the country's three largest companies overall. As a result, many investors — as well as professionally managed funds — anchor their portfolios with one or more of these names.

But which is the best option for your portfolio? Below we take a look at each of them, then come up with a verdict.

The case for RBC

As Canada's largest bank, RBC has plenty of scale, which in banking is a big advantage. For example, RBC has a top two market position in every Canadian banking product. This helps the company absorb its fixed costs more easily than competitors do.

But what really separates RBC from the other banks is its capital markets and wealth management businesses. These are areas where other banks around the world are pulling back, thanks to increasing capital requirements. So this has allowed RBC to gain market share in capital markets and pick up some cheap acquisitions in wealth management.

On the other hand, these two business lines arguably make RBC the riskiest of Canada's Big 5 banks. Earnings can be very volatile, and depend a lot on how stock markets are doing. That is not a problem these days; stock markets are strong and RBC is posting record earnings. But if world events turn the wrong way, RBC shares could easily lag its peers.

The case for TD

TD has quite a different focus than RBC, preferring to hone in much more on retail banking. TD is also much more focused on the United States — most Canadians don't realize that TD has more branches south of the border than it does in Canada.

The U.S. banking environment isn't ideal right now, but with a continuing U.S. recovery — and eventually some higher interest rates — TD has plenty of opportunity to grow earnings. Better yet, its focus on retail banking makes its earnings less volatile than RBC's.

The one problem with TD shares is its price. Trading at over 14 times earnings, it is the most expensive of the Big 5. It seems that the bank's positive attributes are already priced into the stock.

The case for The Bank of Nova Scotia

The Bank of Nova Scotia has a focus entirely different from that of RBC and TD, preferring to aim much of its efforts on emerging markets, especially Latin America — in fact only about half of net income comes from Canada, the lowest share of any bank in the country.

This certainly comes with risk: The Bank of Nova Scotia itself has had some misadventures in countries like Argentina and Mexico. But at the same time, the bank is also very well suited to grow earnings. And it is expending its effort in Mexico, Colombia, Peru, and Chile, four countries with very healthy, growing economies. Better yet, the shares trade at only 12.4 times earnings, making it the cheapest of the Big 5.

The verdict

At this point, The Bank of Nova Scotia seems to be the most compelling option. But then again, they all have their positive attributes and focus on different areas. So there's also a strong case to hold all three companies.

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