Why Low Oil Prices Make Toronto Dominion Bank a Buy

Description

After OPEC recently decided to maintain production at 30 million barrels of oil daily, the price of crude has plunged on the back of declining demand and global oversupply to new lows. This now sees West Texas Intermediate or WTI and Brent trading at their lowest prices since 2009.

While this may be bad news for Canada's energy patch, it is fast shaping up as good news for Canada's largest bank by assets **Toronto Dominion Bank** (TSX: TD)(NYSE: TD).

Why lower crude prices benefit Toronto Dominion

With growth prospects for the big six significantly constrained at home because of Canada's relatively small and over-saturated financial services market, it is those banks with significant offshore exposure that have the best growth opportunities.

Toronto Dominion has the largest exposure to the U.S. of all of Canada's banks, with around a quarter of its net income derived from its U.S. operations. These operations consist of traditional retail and commercial banking as well as wealth management and securities business.

Already this year the U.S. economic recovery has continued at a startling pace — third quarter 2014 GDP came in at a very healthy 3.5% well above the 3% originally and forecast. Significantly lower crude prices will act as a windfall for consumers and small business owners at the pump.

This makes them a tailwind that will drive further U.S. economic growth by stimulating consumer spending and small business through cheaper gasoline and energy prices.

Both of those sectors received little real benefit from the Fed's policy of quantitative easing, and increased consumer spending and small business activity is a real boon for the U.S. economy. This will help to boost employment and wages, with real wage growth continuing to lag with median income down by 5% from the peak hit in 2007. In turn, this will stimulate demand for credit and other banking products including insurances and wealth management, boding well for further earnings growth for Toronto Dominion.

For its fiscal third quarter, Toronto Dominion's U.S. retail operations saw net interest income pop by 2% quarter-over-quarter and 4% year-over-year. This was on the back of total loans under management having shot up a healthy 2% quarter-over-quarter and 14% year-over-year.

Such healthy loan growth was achieved on the back of the U.S. economy expanding at an estimated 2.6% for the full-year 2014. With it expected to grow by 3.5% in 2015, this loan growth can only continue at a stronger rate. Further, lower crude prices are triggering a rethink among analysts and economists as to how much more economic growth will be seen in the U.S. in 2015.

While Toronto Dominion is worried about the outlook for the domestic market and will more than likely implement measures to drive efficiencies at home, its U.S. operations appear to be in the cusp of taking off. With a strong U.S. economic recovery spurred on by significantly lower crude prices set to drive higher employment and incomes as well as greater business activity set to drive higher demand for credit.

CATEGORY

1. Bank Stocks
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