



Which Is a Better Play on the U.S. Economy: Bank of Montreal or Toronto-Dominion Bank?

Description

There is no doubt about it—Canada is not the best place in the world to be investing right now. In fact, even in good economic times, the TSX is an extremely undiversified and volatile index, with well over half the index being comprised of financial and energy stocks.

This is, in many ways, a reflection of the broader economy, and with the price of West Texas Intermediate crude down 35%, an extremely over-leveraged Canadian consumer, and a housing market that could be over 30% overvalued, the Canadian economy is lagging behind the U.S. on numerous indicators.

According to a recent OECD report, the Canadian GDP is expected to grow only 1.5% in 2015, compared with their prediction of 2.4% for the U.S. economy. This is the reason why banks like **Bank of Montreal** ([TSX:BMO](#))([NYSE:BMO](#)) and **Toronto-Dominion Bank** ([TSX:TD](#))([NYSE:TD](#)) are—quite wisely—looking south for earnings growth. In doing so, they provide Canadian investors the opportunity to capitalize on higher GDP growth, a U.S. consumer that is significantly underleveraged compared with Canada, and a country that is a net importer of oil.

The question for investors is, which bank is a better way to gain this exposure?

BMO and TD by size of American operations

The first way to examine this is by looking at the size of both companies' operations. For BMO, the bank regularly states in presentations that approximately 17% of adjusted net income comes from their U.S. Personal and Commercial segment. However, it is important to note that BMO also has both their Wealth Management and Capital Markets divisions operating in the U.S.

On an adjusted net income basis, BMO earned approximately \$1.14 billion in Q2 2015. In total, BMO's combined U.S. operations earned about \$268 million in Q2, making their combined U.S. segments approximately 23.3% of earnings. Most of this (81%) is from their Personal and Commercial segment, whereas about 7% comes from Wealth Management and the remainder from their Capital Markets

segment.

TD Bank, on the other hand, earned approximately \$2.1 billion in Q2 2015. Overall, their U.S. retail segment earned approximately \$626 million, meaning about 29% of net income overall originates from their U.S. operations. Like BMO, TD also has a Wholesale Banking segment, which has U.S. exposure, but TD does not clearly state which portion of these earnings comes from the U.S.

It is, however, fairly safe to say that while TD and BMO have similar-sized U.S. operations, TD has a slight edge.

Quality of geographic exposure

While both banks are similar in the sense that they obtain over a quarter of net income from the U.S., they differ significantly in how they approach the U.S. geographically. Given that the U.S. economy differs dramatically depending on location, one bank may have an edge depending on how they are distributed.

In this regard, TD seems to have an edge. TD has largely concentrated their U.S. operations in the eastern region of the country, and there are numerous benefits to doing so. TD has positioned itself in seven of the 10 wealthiest states, and five of the 10 top metropolitan areas. With 55 million customers within five miles of TD branch locations, TD has positioned itself in some of the strongest, highest-growth U.S. economic regions near plenty of customers. The company is focused on high-growth markets such as New York, Boston, and South Florida, and the company currently has over 100 branches in New York City.

BMO is largely focused on the Midwestern U.S., with operations in Indiana, Wisconsin, Illinois, Missouri, and Arizona. These states, however, are significantly less wealthy than the states where TD operates. In fact, all the states in which BMO operates have household income of \$50,502, which is lower than the median. These states also have heavy exposure to manufacturing, especially Illinois and Indiana, which have been hit extremely hard over the past 15 years due to the collapse of American manufacturing.

With this in mind, TD offers higher quality geographic exposure.

CATEGORY

1. Energy Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:BMO (Bank of Montreal)
2. NYSE:TD (The Toronto-Dominion Bank)
3. TSX:BMO (Bank Of Montreal)
4. TSX:TD (The Toronto-Dominion Bank)

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Author

amancini

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