



Is Toronto-Dominion Bank Set to Make Another Acquisition?

Description

Toronto-Dominion Bank ([TSX:TD](#))([NYSE:TD](#)) has significantly outperformed its Canadian banking peers over the past 10 years, and one of the reasons is due to TD's acquisition-focused strategy.

Since 2005, TD has invested over \$22 billion in acquisitions to aggressively expand its presence in the U.S. marketplace. In May, TD announced a purchase of **Nordstrom's** \$2.2 billion U.S credit card portfolio. In 2013, TD purchased **Target's** \$5.9 billion credit card portfolio, a U.S. wealth management firm, and half of **CIBC's** Aeroplan Visa Portfolio.

Recently, TD's CEO Bharat Masrani indicated that the bank is examining further acquisitions in the U.S. Here's why TD may acquire soon, and what an acquisition may look like.

TD has ample resources and the strategic drive to make an acquisition

TD's CEO has stated that more acquisitions in the U.S. marketplace are currently on the company's radar, providing they make sense both strategically and financially. At the moment, TD not only has the resources to make an acquisition in the U.S., but the right acquisition could help TD better use its balance sheet to expand margins.

Currently, TD's Common Equity Tier 1 (CET1) is sitting at 10.1%—the highest in several years. This ratio basically indicates how well capitalized the bank is, or how much of the bank's assets (like loans or securities) are owned by shareholders as opposed to depositors and other lenders.

As TD continues to generate strong profits, it retains more earnings and, as a result, its capital position continues to expand. Eventually, there will come a need to deploy excess capital to make sure shareholders are getting adequate returns, and acquisitions are an effective way to do so.

In TD's U.S. retail segment, the need to deploy capital is even more pressing. Thanks to TD's incredible deposit franchise in the U.S., TD is currently in a position where its deposits actually exceed its loans by a decent margin. As a result, TD needs to invest in more liquid assets like securities or cash, which offer lower yields.

An acquisition could help TD acquire more higher-yielding assets, like loans, which would help them earn a better spread on their deposits.

TD could consider another U.S. credit card-portfolio acquisition

One acquisition option, according to TD's CEO, is to expand further into the credit card space. Currently, about 5% of TD's total loans are from credit cards, and TD's CEO has stated this is well within the concentration they are comfortable with, which means there is room for expansion.

Credit card acquisitions are particularly attractive because credit card assets are very high yielding. While these assets are riskier and have higher loan losses, the high interest rates charged mean that even factoring in the higher loan losses, credit cards lead to much higher return on equity than other types of loans.

For TD, this effect may be amplified, because TD has most of its deposits in low-cost chequing and saving accounts. Buying more credit card portfolios gives TD the chance to invest those deposits into high-yielding credit card assets.

TD could follow BMO's footsteps

Recently, **General Electric** announced that it will be selling off its finance assets, and **Bank of Montreal** just took advantage by purchasing its \$11.5 billion transportation finance business. This transaction will add to BMO's earnings, increase BMO's U.S. presence, and improve margins.

Over the next year or two, General Electric will continue to sell off its finance assets, and TD has been widely considered to be a potential buyer. Such an acquisition would allow TD to deploy its excess U.S. deposits into higher-yielding loans, while allowing TD to further diversify away from Canada and strengthening its overall growth profile at a time when overall growth is slowing.

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