Why Toronto-Dominion Bank Stock Is Lower Risk Than Royal Bank of Canada

Description

Royal Bank of Canada (TSX:RY)(NYSE:RY) and **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD) are not only Canada's two largest banks, they are the country's largest companies. So it's no surprise that so many Canadian investors hold both stocks.

And while they are both large Canadian banks, there are actually some big differences between the two. We take a closer look at three of these differences, and reveal why TD is the safer bank to hold.

1. A difference in geography

The table below shows the geographic breakdown of RBC's and TD's loans.

	RBC	**TD**
Prairie Loans	19%	12%
Ontario Loans	36%	40%
Rest of Canada	30%	17%
U.S.A	8%	31%
Rest of World	7%	0%
Total	100%	100%

As can be seen, TD is heavily concentrated in Ontario and the United States, while having relatively little exposure to the Prairie Provinces. And in today's environment, this is important. Alberta's economy is struggling mightily with low energy prices, and this could lead to significant loan defaults in the province.

Meanwhile, Ontario is benefiting from low oil prices and a cheap Canadian dollar, which is great news for TD. And down in the United States (especially where TD is concentrated), consumers and businesses aren't spending so much money on gasoline. This puts extra money in their pockets, which should mean fewer loan defaults. So if you're afraid of the low oil price and its effect on the banks, you can see there's much less to worry about with TD.

2. A difference in business models

RBC has a very diversified business model, while TD is mainly a retail bank. To be more specific, over 20% of RBC's income comes from capital markets, while this number is less than 10% for TD.

Again this makes a difference, because the capital markets are a cyclical, high-risk, opaque business. And retail is far steadier by comparison. So if the energy sector does wreak havoc on the Canadian economy, RBC is certainly more exposed.

3. A difference in approach

Ever since 2002, which was an awful year for TD, the bank has placed special emphasis on risk management. And this paid off in a big way during the financial crisis. TD also has strongly emphasized customer service. Clearly, the bank wants to make money the old-fashioned way.

RBC is no slouch when it comes to risk management and customer service. But it is no TD, and that may become a problem if Canada's economy continues to suffer.

TD trades at 11 times earnings compared to only nine times for RBC, so TD's lower-risk stock does come with a price. But given the precarious state of Canada's economy, the premium is well worth it.

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