

Short Toronto-Dominion Bank at Your Peril

Description

It seems like investors are quite bearish on **Toronto-Dominion Bank** ([TSX:TD](#))([NYSE:TD](#)).

According to the latest report from the Toronto Stock Exchange, TD is Canada's second-most heavily shorted stock with investors betting against more than 84.2 million shares. Based on the current share price of the company, a collective \$4.4 billion is betting on shares of Canada's second-largest bank to go down.

And remember, TD Bank is inter-listed, which means U.S. investors can bet against shares that trade on the New York Stock Exchange. According to the latest report from south of the border, an additional 6.8 million shares are being actively shorted by investors in the United States.

What exactly is behind this bearish sentiment for a company that has been a terrific long-term investment? Let's take a closer look.

Canadian problems

Last year was tough for the Canadian economy, and 2016 doesn't look like it'll be much better.

It seems like every commodity was down, especially crude oil. Not only does a bank like TD have billions lent out to energy producers, but it has additional billions in mortgages and consumer loans to folks who work in the sector.

Weakness in Alberta has been well documented. Borrowers in the province are starting to default at alarming rates. Folks with underwater mortgages are starting to mail their keys back to the bank, taking advantage of Alberta's non-recourse mortgage laws. Unlike every other province in Canada, borrowers in Alberta cannot be sued personally if they default on their mortgage. The lender can only go after the equity in the house.

This trend isn't lost on other investors. For most of 2015, hedge funds crowded into what was dubbed as the "short Canada" trade. The theory was the unraveling of commodity markets would hit Canadian lenders hard. The weakness in the economy would then hit real estate prices, popping the bubble which has gotten so much press.

But so far, this isn't happened. Sure, shares of TD are down over the last year, but only about 5%. And for the most part, housing prices have held up pretty well with the exception of a few places that have been really hit hard by crude's decline, like Fort McMurray. Loan-loss provisions have barely crept upwards as oil companies and their employees have been able to stay afloat. And strong results from the company's U.S. division have helped offset any weakness from Canada.

Problems with Canada's economy could easily get worse. In fact, I'd argue it's almost a given they do. But at the same time, TD is a diverse financial institution with operations across Canada and in the United States. It's spread out and intelligently managed. It'll survive this crisis.

One picture says a thousand words

Over the last 20+ years, it hasn't been a good idea to bet against TD Bank. Courtesy of Yahoo Finance, here's how TD performed from 1995 to today:

TD Bank 1995-2016

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Over the last 21 years TD has dealt with the rise and collapse in the tech bubble, the giant fraud which was Enron, 9/11, the financial crisis of 2008-09, and at least two North American recessions. And yet shares are still up approximately 1,000% since the beginning of 1995, and that's even before counting dividends.

Or, to put it another way, if you had stuck \$100,000 in TD shares back on February 17, 1995 and forgot about them this whole time, you'd be sitting on an investment worth more than \$1.7 million today if you had reinvested all dividends.

Why anyone would bet against a company with that kind of history is beyond me. Sure, there are some pretty major dips in that price chart, especially during 2008-09. But not only has TD recovered—it's prospered.

If Canada continues to be weak, TD shares could sink farther. Over the short term, betting against the company could work. But as an investment over the next few decades, you're nuts to bet against TD. Investors should take advantage of the weakness to buy shares to tuck away for a very long time.

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