Why You Should Wait to Buy Toronto-Dominion Bank

Description

Toronto-Dominion Bank (TSX:TD)(NYSE:TD) shares had a difficult year in 2015—shares ended the year down about 2.3%. Despite this, however, TD just released full-year results for 2015, and results were strong. The bank reported earnings growth of 8% (within its target range of 7-10%) and was above its peer group average of 6%.

This included 6% growth from its Canadian Personal and Commercial segment (once again, well above the peer group average), and this is despite the fact that oil prices plunged significantly in 2015 and the Canadian economy performed poorly.

Strong earnings performance mixed with poorly performing shares seems like an excellent buying opportunity, and it was for investors who entered a month ago. TD shares have rallied a huge 13% in the past month alone. At current levels, however, TD seems to have much more downside than upside. Fortunately, however, investors may get another chance to enter TD at a lower price level and therefore get a much higher return.

TD shares may still have upside, but there is also downside risk

Investors following Canadian banks recently may have noticed that Canadian bank shares (including TD) have begun to closely track the price of oil. In fact, WTI crude oil prices formed their bottom at about $26 per barrel, and on the same day TD formed its most recent bottom at $48.50 per share.

Since then, both oil and TD have rallied, and both recently hit their previous highs not seen since late December 2015. With this in mind, TD may need oil to move higher in order for its shares to move higher. While oil prices will likely move higher over the course of 2015, many believe the current rally that has been in place for the last month may be nearing its end. This means investors may get another chance to buy TD shares.

In addition to this, TD shares are also looking like they are becoming fairly valued. **RBC** estimates that TD will earn $4.75 per share for 2016, which gives TD forward price-to-earnings ratio of 11.59. Overthe past 10 years, TD has traded at an average forward price-to-earnings ratio of 11.6, which meansthat the bank is currently trading at average levels.

The bank does have upside from these levels. TD has some of the lowest oil and gas loan exposure of its peers. In addition to this, TD also has a better growth outlook than its peer group. As a result, it could trade at a premium to its peer group with a price-to-earnings ratio of 12 or possibly higher. This could give TD a few more dollars of upside.

Waiting to buy is a better idea

Rather than buying now and possibly gaining a few dollars per share, it is better to wait for TD shares to pull back and then buy at a lower price level. This will not only provide more upside, but it could also be less risky, since TD shares would be trading at a lower level.

The question is, will TD shares actually pull back? It is impossible to say for sure, but given that TD shares have been extremely correlated to the price of oil, it is likely that if oil prices fall from here, TD shares will also fall from here.

There is good reason to think that oil prices are set for a pullback. There is still a global oversupply of about 1.5-2 million barrels per day, and U.S. crude oil inventories are currently 163 million barrels higher than the 2010-2014 average (and about 73 million barrels above levels at this time last year).

While low prices will eventually drive U.S. production out of the market and lead to higher prices, the oversupply still exists, and Iran is unlikely to agree to any production cut. This means oil prices could fall again and likely take TD shares with it, giving a good buying opportunity to investors who missed the first rally.

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