Toronto-Dominion Bank Raises Prime: What's the Bottom Line?

Description

The news that **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD) was raising its mortgage prime rate by 15 basis points to 2.85%, effective immediately, spread like wildfire Tuesday as Canadians pondered how this would personally affect them.

Investors, on the other hand, wondered what this interest rate hike would mean for TD and the other four major Canadian banks.

Two words—more money!

Before I get into the finer points of how the banks benefit, let me remind readers that this rate hike by TD only affects variable rate mortgages and not fixed-rate customers. Nor does it affect lines of credit, etc.

This is simply directed at covering the bank's rising costs as a result of the four rules being implemented by the federal government to ensure Canada doesn't experience a housing crisis like the one our neighbours to the south lived through between 2007 and 2009.

At this point, none of the other big banks have followed suit, but it's expected that they will. For this reason, I'll examine all five businesses to see exactly how they'll benefit from this seemingly insignificant rate hike.

TD Bank

- The bank's total loan portfolio at the end of October 2015 was $564.4 billion.
- Its Canadian residential mortgages accounted for $185 billion, or 33% of its total loan portfolio.
- Approximately 62% of its loan portfolio had maturities of one year or longer, making them sensitive to rate increases. Those are the ones we're interested in.
- Of the $349.9 billion, only about $105.0 billion, or 30%, are variable rate loans with the rest fixed-rate in nature. Those aren't affected by the hike.

Mortgages affected = $55.5 billion ($185 billion multiplied by 30%)

Additional income = $83.3 million ($55.5 billion multiplied by 0.15%)

Royal Bank of Canada (TSX:RY)(NYSE:RY)

- The bank's total loan portfolio at the end of October 2015 was $474.3 billion.
- Its Canadian residential mortgages accounted for $228 billion, or 48%, of its total loan portfolio.
- Approximately 37% of its loan portfolio had maturities of one year or longer.
- Of the $175.5 billion, only about $66.7 billion, or 38%, are variable rate loans.

Mortgages affected = $86.6 billion ($230 billion multiplied by 38%)

Additional income = $130.0 million ($86.6 billion multiplied by 0.15%)

Bank of Nova Scotia (TSX:BNS)(NYSE:BNS)

- The bank's total loan portfolio at the end of October 2015 was $462.8 billion.
- Its Canadian residential mortgages accounted for $190 billion, or 41%, of its total loan portfolio.
- Approximately 62% of its loan portfolio had maturities of one year or longer.
- Of the $286.9 billion, only about $67.6 billion, or 44%, are variable rate loans.

Mortgages affected = $83.6 billion ($190 billion multiplied by 44%)

Additional income = $125.4 million ($83.6 billion multiplied by 0.15%)

Bank of Montreal (TSX:BMO)(NYSE:BMO)

- The bank's total loan portfolio at the end of October 2015 was $335.9 billion.
- Its Canadian residential mortgages accounted for $97 billion, or 29%, of its total loan portfolio.
- Approximately 58% of its loan portfolio had maturities of one year or longer.
- Of the $195.9 billion, only about $94 billion, or 48%, are variable rate loans.

Mortgages affected = $46.6 billion ($97 billion multiplied by 48%)

Additional income = $69.9 million ($46.6 billion multiplied by 0.15%)

Canadian Imperial Bank of Commerce (TSX:CM)(NYSE:CM)

- The bank's total loan portfolio at the end of October 2015 was $291 billion.
- Its Canadian residential mortgages accounted for $162.7 billion, or 56%, of its total loan portfolio.
- Approximately 64% of its loan portfolio had maturities of one year or longer.
- Note: CIBC doesn't seem to present the breakdown of loans between variable and fixed-rate, so I've taken the average of the other four banks, which is 40%. Therefore, of the $186.2 billion, only about $74.5 billion are variable rate loans.

Mortgages affected = $65.2 billion ($163 billion multiplied by 40%)

Additional income = $97.8 million ($65.2 billion multiplied by 0.15%)

The winner

The winner depends on whether you look at the additional income generated from the 15-basis-point increase in variable rate mortgages in total dollars or the percentage that income represents of the bank's total loan portfolio.

In addition, this is the prime rate and does not necessarily apply to every variable mortgage a bank might have, so the ultimate number could be much lower. It's simply meant to give an idea of what this move might mean for shareholders.

Therefore, in total dollars, Royal Bank would benefit most at $130 million.

However, if you consider the bank’s additional income as a percentage of its total loan portfolio, then CIBC benefits most, followed by Royal Bank, Bank of Nova Scotia, Bank of Montreal, and TD, which is ironic given TD is the one that got this ball rolling.

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Author
washworth