A Lesson From Warren Buffett: How to Play Toronto-Dominion Bank After its "Wells Fargo Moment"

Description

Toronto-Dominion Bank (TSX:TD)(NYSE:TD) got crushed last Friday. The stock plummeted over 5% in a single trading session — the worst plunge since 2014. The decline was caused by a story on how the bank's employees have been breaking the law at the customer's expense in order to meet the needs of the unrealistic expectations put on them by their managers.

Mark Twain once said, "History doesn't repeat itself, but it often rhymes." There's no question that this mistake is awfully similar to the one **Wells Fargo & Co.** (NYSE:WFC) made over a year ago. Many analysts are concluding that Toronto-Dominion had its own "Wells Fargo moment," but is the scandal really going to result in a massive sell-off? Or is this the chance for long-term investors to get in on a company with fantastic fundamentals?

I believe Toronto-Dominion is the strongest Canadian bank by far. The company has a top-notch risk-management strategy and a solid U.S. banking segment that has grown over the last few years. The U.S. banking segment is going to be a gigantic tailwind for the company, as the U.S. economy strengthens. Sure, the bank hasn't been the best performer over the last few earnings reports, but the U.S. banking division is set to take off from here, and when it does, profits will soar and the stock will skyrocket.

Toronto-Dominion is a wonderful business with very strong fundamentals, but it made a big mistake, and the bank has an ugly tarnish on its reputation that could hurt it in the short to medium term.

What would Warren Buffett do?

Warren Buffett felt strongly about his shares of Wells Fargo. He clearly thought it was the best American bank, and he didn't sell a single share during the scandal. Sure, Wells Fargo made a mistake, and it paid the price for it, as the stock plunged over 22% from peak to trough. The stock eventually rebounded in the latter part of 2016, and it looks like the company has moved on from the scandal, which was very similar to the one Toronto-Dominion is experiencing right now.

Both Toronto-Dominion and Wells Fargo made a costly mistake. The management team put forth unrealistic expectations on its lower level employees, and this resulted in a bunch of shady business practices at the customer level. The management team knew what was going on, and it's very likely that CEO Bharat Masrani knew of these issues, but he didn't act on it, and this could cost him his job.

Warren Buffett was confident that Wells Fargo could pull itself out of the mess. Warren Buffett claimed it was a mistake and that the company would need to "…get it right, get it fast, get it out, and get it over." Wells Fargo didn't quite "get it [fixed] fast," but I believe Toronto-Dominion will be able to learn from both its own and Wells Fargo's mistakes and move on.

What should you do?

Toronto-Dominion is still a magnificent business, but this scandal will definitely bring forth a ridiculous amount of volatility over the next few months. The company will be trying to make things right, but it's inevitable that the bank will have some negative short-term effects like slower client growth. I believe the company will get through this, and if you're a long-term investor looking for a core holding in a magnificent company, then you should definitely buy shares on the way down.

Short-term pain for long-term gain

We've seen this story before. Short-term losses will happen, but the bank will eventually get over this mistake. Mr. Masrani let this thing get out of control, and I'd be very surprised if he keeps his job after this is all over.

I haven't sold a single one of my shares, and I will be buying more on the way down.

Stay smart. Stay hungry. Stay Foolish.

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