Ignore the Crisis at Toronto-Dominion Bank: Buy the Dip

Description

I'm always amazed by how investors react to crisis-driven headlines dripping with sensationalism. The latest to stir panic among investors are claims that **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD), Canada's second-largest bank by assets, has acted unethically and, in some cases, illegally in the sale of financial products. There have been admissions from some employees to this effect.

There are now comparisons being drawn between this scandal and the US$185 million scandal that engulfed major U.S. bank **Wells Fargo & Co** (NYSE:WFC) in September last year.

The allegations have led to Canada's largest financial services ombudsman to apply greater scrutiny to the industry. This couldn't come at a worse time for Toronto-Dominion. Like the other major banks, it has been battling to grow its market share in an over-saturated domestic market which is afflicted by minimal growth opportunities as it reels under the impact of weak economic growth.

While the scandal has certainly harmed Toronto-Dominion's brand and reputation, causing its share price to plunge by almost 5% in recent days, there is no need for investors to panic. As a former banking professional, I expect the long-term damage to be negligible at worst.

Now what?

We only need to turn to Wells Fargo to see that despite the damaging headlines and admissions which caused its stock to plunge to under US$44 per share, it has rallied strongly to be up by 17% over the last year.

I expect a similar outcome for Toronto-Dominion.

Canada's banks have a history of resilience, bouncing back from any crisis. They weathered the Global Financial Crisis in great shape, and because of Toronto-Dominion's strengths, it will emerge from this catastrophe as well.

Among the key strengths that will allow the bank to do so is its wide economic moat; in conjunction with the bank operating in a highly regulated and oligopolistic industry, this moat protects the bank from competition, virtually assuring earnings growth.

There are also a number of powerful tailwinds that will drive earnings higher in coming months.

Crucial among them is the increasingly upbeat economic outlook south of the border.

As the 10th largest U.S. bank, Toronto-Dominion is certainly well positioned to benefit from a stronger U.S. economy. U.S. GDP is expected to expand at between 2% and 3% during 2017, which is a solid increase over the 1.9% reported for 2016.

Trump's plans to reduce regulation in the financial services industry will reduce costs and make it far easier for banks to do business; along with a rate hike, this will boost margins for banks operating in the U.S.

Because Toronto-Dominion's U.S. retail banking business is responsible for generating almost a third of its net income, each of these factors will give the bank's bottom line a healthy lift.

Investors would also do well to remember that this issue relates to allegations of miss-selling and questionable conduct; it doesn't bring into question the quality of Toronto-Dominion's fundamentals. The bank possesses a high-quality loan book with net impaired loans only representing 0.45% of its total loans.

Furthermore, it remains well capitalized with a common equity tier one capital ratio of almost 13%.

So what?

While such events are certainly unpleasant for investors, the long-term impact will be inconsequential. For the reasons discussed and more, Toronto-Dominion will keep growing, unlocking value for shareholders and rewarding them with regular dividends hikes. Toronto-Dominion yields a tasty 3.5%.

Let's not forget that since the Global Financial Crisis, when the naysayers were out in force, and Toronto-Dominion's shares plunged to under $19, its stock has almost quadrupled in value. This highlights that now is the time for investors to take advantage of its weak share price and acquire Toronto-Dominion.

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