# Toronto-Dominion Bank Is NOT Severely Undervalued

## Description

**Toronto-Dominion Bank** (TSX:TD)(NYSE:TD) is an incredible business, too cheap to ignore, says Fool.ca contributor Joey Frenette.



Is he right?

While it might be a good business, I suspect "incredible" is a bit of a stretch.

**Amazon.com, Inc.** is a great business. So too, I would argue, is **Tesla Inc.** I would even go as far as nominating **Berkshire Hathaway Inc.**, the holding company Warren Buffett started over 50 years ago.

These are all great businesses.

No bank, I would suggest, qualifies for such a distinction. That's especially true here in Canada, where the competitive marketplace is staked out by a handful of banks propped up by exceptionally bank-friendly mortgage insurance practices.

However, beauty is in the eye of the beholder. He may be right; I may be wrong. Never the twain shall meet.

The second part of Frenette's statement that TD Bank stock is too cheap to ignore is definitely up for debate. Here's why.

### Valuation

Today, TD Bank trades at 13.7 times earnings. That's higher than all four of its peers, including **Canadian Imperial Bank of Commerce** (TSX:CM)(NYSE:CM), which trades at a 28% discount to TD.

So, if TD Bank is too cheap to ignore, it follows that the other four Canadian banks are also too cheap to ignore — a hypothesis I'm not ready to concede given the headwinds faced by all of the banks when it comes to growing their domestic mortgage businesses.

Rising home prices in places like Toronto have made Canadians feel wealthier than they truly are; a

CIBC survey just released found that 54% of Canadians believe housing prices will *never* drop. Never. I wonder why Canadians aren't that short-sighted about stocks.

As interest rates rise, banks make more money. That's the good news.

The bad news is that the real estate market is beginning to look a lot like the Titanic with homeowners scrambling to get seats on the lifeboats before they run out. Only, in the case of real estate, it's Canadians wondering whether they should sell or not.

The last time housing prices corrected in Toronto in a major way was between 1989 and 1996 when they fell by 40%, adjusted for inflation. Between 1985 and 1996, home prices increased by 2.5% annually, adjusted for inflation, about the same as the GDP growth. In 2016, the average house in the Greater Toronto Area jumped by 20%.

You can argue all day long about which bank has best insulated itself from a housing correction, but once those interest rates start rising and homeowners start defaulting on their mortgages or rushing for the exits, Canadian banks aren't going to be able to replace this lost income fast enough to keep profits rising.

TD's valuation, along with all the other banks, is very tenable.



**Bottom line**

News broke April 12 that TD, along with **Royal Bank of Canada** and four other banks, face a lawsuit that they allegedly fixed bond prices in a 10-year collusion scheme to profit from the manipulation of those bond prices.

While these are just allegations at this point, TD is already in the doghouse with Canadians over its overzealous sales practices. These are not the tenets of a great business, and TD is certainly not deserving of a premium multiple, as has been the case historically.

I would argue that only CIBC stock is too cheap to ignore; even then, I'd be careful about buying Canadian bank stocks at this point because the downside appears greater to me than the upside.

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