TD Stock a Buy as Inflation Fears Weigh on Markets

Description

The consumer price index in the U.S. rose 4.2% year over year in April, which was the fastest gain in more than 12 years, according to *CNBC.* This was higher than the 3.6% increase forecast by Wall Street. The higher-than-expected inflation rates have kept investors wary, which has resulted in a volatile stock market this year.

Inflation impacts the life of every individual, as the rising costs of products and services suggest residents may save less and spend more. Rising inflation rates are even more detrimental to retirees who are not working and rely on passive-income streams to foot their bills.

There is a good chance that the Federal Reserve might increase interest rates to offset high inflation, which, in turn, will move institutional and retail investments into asset classes such as bonds. The equity market has historically underperformed other asset classes in periods of high inflation rates.

However, banking companies like **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD) might be good bets if interest rates rise. While the demand for loans might impact top-line growth for TD and peers, the company will benefit from higher profit margins if interest rates increase.

TD Bank is a giant

With a market cap of $160 billion, TD Bank is one of the largest Canadian companies. It is also one of the 10 largest banks in North America and ranks fifth in terms of total assets. TD has more than 2,300 retail locations in the continent with close to $450 billion in assets under management and over $900 billion in total deposits in Q1.

TD Bank is well diversified and the Canadian Retail Bank business accounts for 58% of earnings, followed by U.S. Retail at 18%, Wholesale at 14%, and TD Ameritrade at 10%.

In the last four quarters, TD Bank's net income stood at $12.3 billion, while adjusted net income was over $10 billion, which was the highest among Canadian banks. It ended Q1 with a common equity tier-one capital ratio of 13.6%. The tier-one capital ratio has to be at least 6%, according to Basel III norms.

In Q1, TD managed to increase adjusted net income by 10% to $3.38 billion, or $1.83 per share, which is significantly higher than Bay Street EPS estimates of $1.49. The bottom line was driven higher due to low provision for credit losses that fell $604 million on a sequential basis.

What's next for investors?

TD stock has created massive wealth for long-term investors. In the last five years, it has returned 56% to investors. After we account for dividend reinvestments these returns will be closer to 75%. In the last decade, TD stock has returned 110% easily outpacing the TSX Index, which is up 60% in this period.

TD Bank has robust fundamentals and a strong balance sheet. Its risk-weighted assets were down 2% on a sequential basis in Q1 while it ended the quarter with a leverage ratio of 4.5% and a liquidity coverage ratio of 139%.

TD stock has a forward yield of a tasty 3.6%, which alone should allow you to beat inflation rates over the long term. With approximately $2 trillion in assets and a sizeable presence south of the border, TD Bank aims to expand via accretive acquisitions as well in the U.S.

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