TD Bank Is Great Buy While it’s Still Cheap

Description

TD Bank (TSX:TD)(NYSE:TD) took an uppercut straight to the chin on Thursday following the release of some decent but not incredible quarterly results. It wasn’t just the numbers themselves that caused shares to fall under considerable pressure, ending the day down 2.4%.

In an unexpected move, PM Justin Trudeau’s election campaign recently promised to target the big Canadian banks (and insurers) with tax hikes.

As to why Trudeau is going after the banks, rather than going after the big telecoms to lower mobile, as NDP leader Jaghmeet Singh is promising, is anybody’s guess. In any case, shares of the Big Six Canadian banks may be pricing in a high likelihood of a Liberal government, as we move head-first into election season.

Undoubtedly, the Big Six banks have been tackling a challenging environment over the past five years, with the Canadian credit slowdown that preceded the coronavirus recession. They’ve come a long way since last year, and profits (and dividend hikes) are poised to come flowing in. But is it too soon to dole out take hikes? And would there be negative implications for Canadian consumers and investors in the big banks?

Liberal big bank tax hike talks weigh on TD Bank stock

Certainly not. But it’s a rather prominent thorn in the side of Canada’s top financial institutions, as they look to continue recovering from the horrific pandemic.

Moreover, to compensate for any take increases targeted at them, they may have to increase service fees accordingly. Undoubtedly, commission-free trading, which hadn’t taken off in Canada as it had in the U.S., may not be widely embraced by the Big Six.

Although **National Bank of Canada’s** first move to eliminate trading commissions was encouraging, the pressure doesn’t seem to be on for the bigger players such as TD Bank — at least, not yet.

It seems like any proposed tax increases on the banks could postpone the next leg of the bank rally at some point down the road, perhaps after the election. In any case, don't expect such increases to trigger a broader correction in the Canadian financials. If anything, it's already been mostly priced in after a rough Thursday of trade.

The road ahead still looks very good for TD Bank and its peers

Looking ahead, credit quality and earnings-growth prospects haven't look this good since the rise out of the 2008 Great Financial Crisis. Trudeau's latest jab at the banks could cause TD Bank and the broader basket to lose a bit of a step. But ultimately, valuations still seem way too cheap at these levels.

For the third quarter, TD showed evidence of a robust recovery. Still, the bank lagged its peers and didn't blow away the numbers, as its peers did. Management also commented that its net interest margins (NIMs) could fall under a bit of pressure over the next several months.

Longer term, though, I think TD stock is among the best of deals in the financial sector. The latest quarter underwhelmed, but the stock already trades at a discount to its peers on a price-to-earnings basis. At 10.8 times earnings, TD stock is nothing short of a bargain. It's a relative laggard for now, but the tides will turn once rate hikes finally arrive in the states. Arguably, TD's NIMs will have the most room to run once we enter that much-dreaded rising-rate environment.

For now, fears over Liberal tax raises on the banks and concerns over variants are likely to act as an overhang on the banks. Although negative, I'd treat such event-induced pressure as a long-term buying opportunity.

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