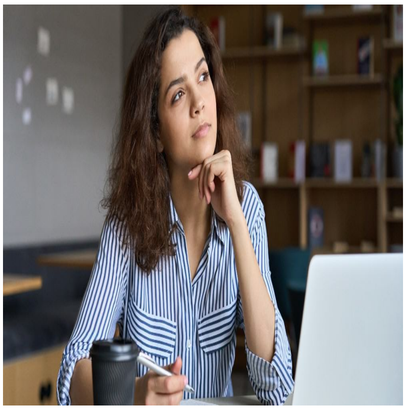

Top February TSX Stock Pick: TD Bank Is a Buy for Passive Income

Description

February has been a rough month for most portfolios so far, but sometimes, you need to be a buyer of TSX stocks when there's blood on the Streets, even if some of it is your own. Undoubtedly, lower prices exist right now, but not all stocks that have been hit are more undervalued than they were before the correction struck. That's why investors should ask themselves whether anything huge has changed about the growth story, the fundamentals, or expectations of the stocks they are considering.

Currently, the dividend giants seem like compelling opportunities for passive income investors who want to stay ahead of inflation, even if central banks are willing to fall behind the curve. Inflation could stick around for longer, punishing savers and bond investors who are too jittery to put money in the equity markets.

Real returns could be harder to come by in 2022

While there's no such thing as "risk-free" in the stock market, I do think that investors, old and young, should weigh the risks of losing purchasing power to inflation against downside risks in the stock market. Indeed, it's getting harder to generate positive real returns (real returns are on an after-inflation basis).

Valuations were high, and arguably, they're still a tad on the high side for select names out there, especially those that didn't fall as hard as the broader markets. With U.S. inflation hovering in the 7% range, one should not rely on central banks acting to bring it back down to the 2% desired range. It could be a tough task to bring inflation back to historical levels. At the same time, bonds may not be a great place, given rate hikes are coming, and they'll surely drag down bond prices, while propelling their yields modestly higher.

It's tough to be an investor. There's no doubt about it. At the end of the day, though, I believe stock investors will be the ones that will come out ahead of this bout of inflation, whether it be temporary or persistent. Yes, rate hikes aren't good for growthy stocks. But there are intriguing sectors that can help you hedge your portfolio against inflation and even generate an impressive real return.

TD Bank and the financials aren't done yet

Financials stocks like **TD Bank** (TSX:TD)(NYSE:TD) are intriguing options when rates rise. Sure, the banks have been leading the broader indexes higher of late. They're hot, with considerable momentum behind them. That said, stronger results and fundamentals have supported the rally. They're wildly profitable, and they're poised to become even more profitable with time as rates surge. Indeed, financials are a new class of momentum stocks that aren't just going to implode once the Fed says it needs to get more aggressive with its rate hike schedule!

Further, TD and the Big Six are some of the highest quality financials in Canada. They've made it through horrid times. Now, they're ready to feel a bit of wind to their back. And I think their earnings can keep their respective price-to-earnings multiples low, even as their share prices rise at an attractive rate.

There's some positivity baked in with the big banks. But I'd argue that the bar isn't as high as it could be, given the economy could be a lot stronger than expected, allowing the Fed the flexibility to raise the bar on rates. Robust economic growth and higher rates are a perfect combo for the banks.

TD Bank is my top pick in the space currently for its rock-solid balance sheet and its sensitivity to higher rates. As loan growth increases alongside rates, the firm could see margins and revenues surge. The result? Huge profits, big dividend hikes, buybacks, and perhaps a big acquisition south of the border.

TD Bank ready to rally higher

TD has made its M&A intents clear. It wants to make a splash, perhaps in the U.S. retail banking space. If TD can't find value, expect more dividend raises.

It's not just positive macro factors that have me bullish on TD stock. The bank could regain its rich premium over its Big Six peers. Indeed, a lot of positive forces are compressing TD's price-to-earnings multiple. Such forces, I believe, will propel the stock steadily higher in a year where growth stocks could sink lower. Even as growth sinks, don't expect the banks to care much. This is an environment where banking on the banks is wise for all investors looking for sizeable real returns.

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