Market Perspectives Q3 2019

TD Wealth Asset Allocation Committee (WAAC) Overview

- Overweight equities and underweight fixed income
- Expect "lower for longer" rate environment to continue with inflation low and central banks accommodative
- Corporate credit benefiting from strong free cash flow and low default risk
- We anticipate a protracted conflict between China and the U.S. on issues of trade and technology leadership
- Episodes of volatility may be driven by trade frictions and slowing global growth

Market Outlook

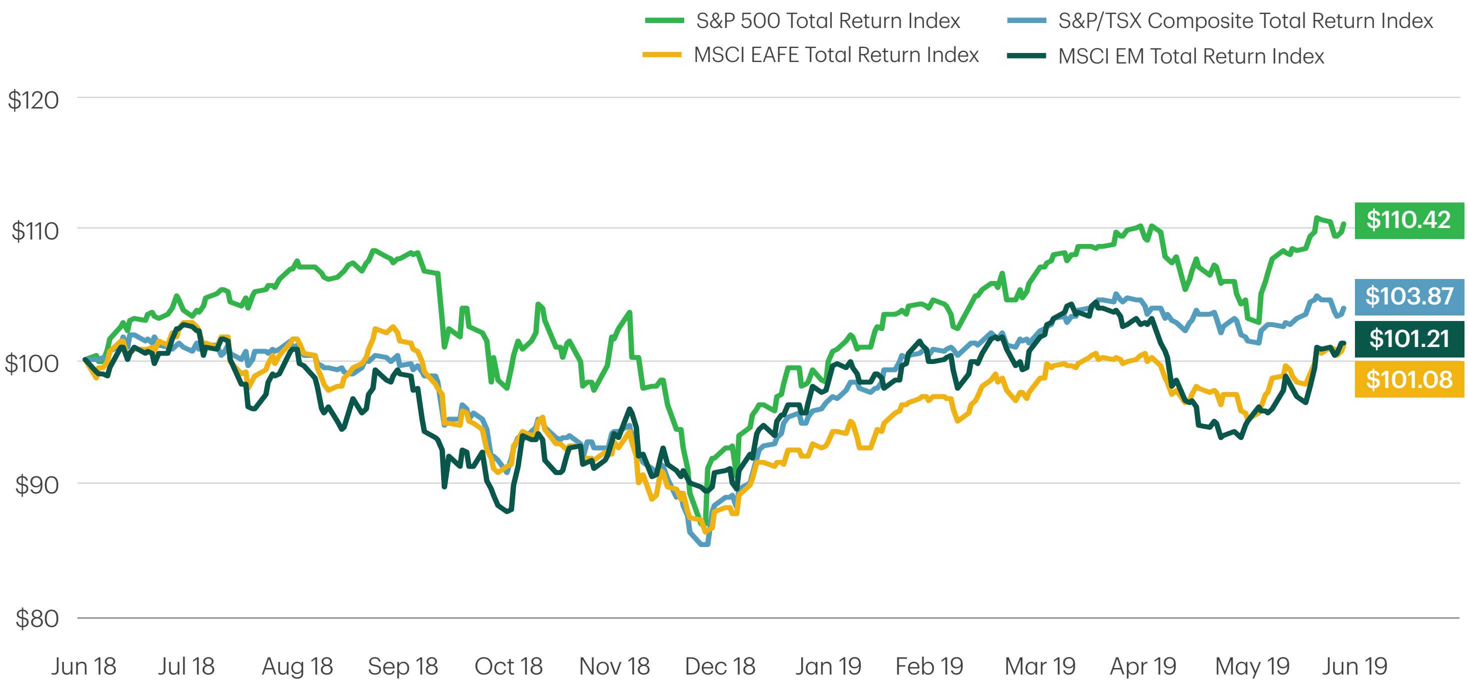
Global Equities Resilient Despite Growing Headwinds

For much of 2019, equity markets enjoyed a resilient rise, bolstered by supportive central bank policies, and optimism over a possible trade deal between the U.S. and China. The S&P 500 Index entered May at an all-time high, but abruptly reversed course as the U.S. announced significant punitive tariff increases on goods imported from China. As a result, global equites sold off in May, trimming some of their 2019 gains. While markets bounced back to reach fresh highs in June, the contentious U.S-China trade dispute, evidence of slowing global growth, and other geopolitical risks have many fearing negative market consequences.

In Canada, the S&P TSX Composite Index gained during the second quarter but was not immune from the brewing trade conflict, waning global economic expansion and poor Energy sector performance (which represents approximately 20% of the Index). Oil prices gave back some of their first quarter gains, hampered by elevated inventory levels and slowing global demand concerns. However, tensions between the U.S. and Iran helped spur a June rally and supported oil prices above 2018 year-end closing levels. The largest component of the index, Financials (roughly 34%), helped drive positive performance during the second quarter.

Despite the challenging economic backdrop, most major equity markets around the world, including Canada and the U.S., delivered returns in the mid-to-high teens for the first six months of the year. Strong labour markets, growing wages, and the low interest rate environment continued to support Price-To-Earnings multiples at higher than historic levels. In addition, there have been fewer excesses in this cycle compared to the previous two, meaning fewer imbalances that may need to be corrected. The WAAC continues to believe that recessionary risks remain low for North America. Slow growth, not zero growth, is our expectation, and this should allow corporate earnings to expand - albeit modestly. Markets have been strong this year, so periods of consolidation should not come as a surprise.

Index Returns Over the Past 12 Months — The Growth of $100



Source: Bloomberg Finance L.P. As of June 30, 2019.

Canadian Bank Earnings in Focus

Canada's Big Six banks delivered a mixed bag of second-quarter results, but collectively generated roughly $12 billion in earnings. Earnings Per Share (EPS) grew at about 4%, with the Toronto Dominion Bank leading the group with EPS growth of 8%. Of note, loan and deposit growth has slowed in the core Personal and Consumer Banking businesses across the group, which reflects slower overall growth of the Canadian economy. Interest margins expanded year-over-year, but this could change should interest rates continue to decline. Credit quality also showed some weakness but remains solid and capital levels are also very strong. With stable capitalization and conservative books, Canadian banks have been ranked among the soundest across the globe by the World Economic Forum.

A recent stress test conducted by the Bank of Canada concluded that large Canadian banks would be well-positioned to manage a sharp repricing in financial markets and a significate housing market correction, should one occur. The share of Canadians falling behind on debt payments is still low and relatively steady.

Overall, we remain comfortable with Canadian banks as core holdings in our Canadian equity portfolios. In this low interest rate environment, generating income continues to be a key theme for investors and we believe that Canadian banks will be able to increase their dividends over time, given their exceptionally diversified earnings mix.

Canadian

The "Big Six" Comparable Second Quarter 2019 Results[1]

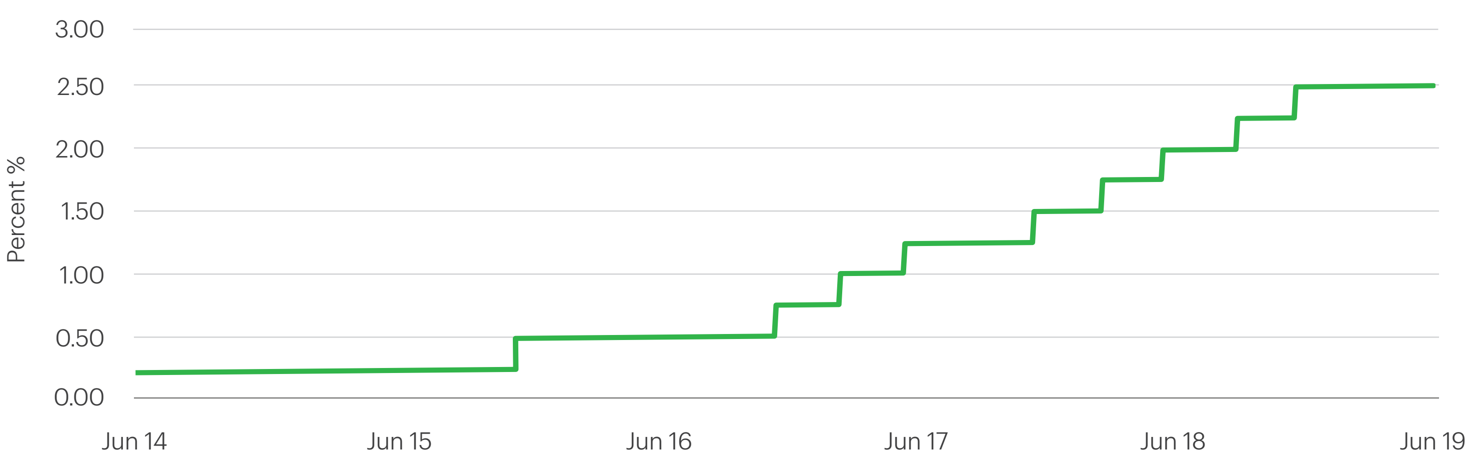
Q2 Quarter Ending April 30, 2019	Adjusted Net Income ($ billions)	Adjusted Net Income Growth (YoY)	Adjusted Diluted Q2 EPS	Adjusted EPS Growth (YoY)	Adjusted Return on Equity	Dividend Yield as at 6/25/19
TD Bank	$3.20	**6.4%**	$1.75	**8.0%**	17.0%	3.9%
Royal Bank	$3.22	**5.9%**	$2.23	**6.2%**	17.8%	3.9%
Bank of Montreal	$1.52	**4.0%**	$2.30	**4.5%**	13.9%	4.2%
CIBC	$1.32	**0.5%**	$2.97	**0.7%**	15.9%	5.3%
Bank of Nova Scotia	$2.12	**3.2%**	$1.70	**-0.6%**	18.7%	4.9%
National Bank	$0.54	**3.3%**	$1.51	**4.9%**	17.8%	4.4%

Central Bank Policy — From Hawk to Dove

At its June meeting, the U.S. Federal Reserve (the Fed) maintained the federal funds rate at a range of 2.25-2.50%. The decision to keep rates unchanged came amid moderating economic expansion and muted inflation. While the U.S. economy continues to be on solid footing, there is evidence it is expanding at a slower pace compared to 2018. Both overall inflation and core inflation, which excludes the cost of food and energy, have declined, and are now running below the Fed's 2% range over a 12-month basis.

Federal Reserve Chair Jerome Powell highlighted a readiness to respond to heightened downside risks with new easing measures, should the economy require support. In its comments, the Fed stated that business investment is slowing, uncertainty has increased, and the U.S. economy is growing at a “moderate” pace. Recent Fed meetings have brought its hawkish three-year drive to tighten monetary policy to an abrupt end, as projections for interest rate hikes for the remainder of 2019 have been abandoned. In fact, many market analysts are now predicting the Fed will lower rates as early as its next meeting.

U.S Federal Funds Rate



Source: Bloomberg Finance L.P. As of June 30, 2019.

In May, the Bank of Canada (BoC) also held its benchmark interest rate steady at 1.75%. Job growth remains on strong footing, and the BoC expects consumer spending, exports and overall growth in business investment to remain stable. The recent escalation of trade tensions has added to economic uncertainty with trade restrictions introduced by China directly impacting Canadian exports. On the other hand, the removal of steel and aluminum tariffs along with positive developments on the expected ratification of CUSMA (Canada-United States-Mexico Agreement) should benefit Canadian exports and investment.

The BoC stated that "the degree of accommodation being provided by the current policy interest rate remains appropriate." Additionally, the BoC reiterated it will remain data dependent and closely monitor developments in household spending, oil markets and global trade, before determining the direction of future rate moves. Finally, it expects inflation to remain near their 2% target for the foreseeable future.

Bank of Canada Overnight Rate Target

Source: Bloomberg Finance L.P. As of June 30, 2019.

WAAC Positioning and Outlook

There remains widespread concern about the strength of the global economy and pessimism over the general health of markets. As we've stated previously, one of the pillars of the WAAC's view on equity markets in 2019 has been that the economy would slow, but North America would not enter a recession. We expect the economy to be strong enough for corporate earnings to continue expanding, albeit at a more modest pace compared to 2018.

Equities

- **NEUTRAL** Canadian equities
- **MODEST OVERWEIGHT** U.S. equities
- **MODEST UNDERWEIGHT** international equities
- **MODEST OVERWEIGHT** emerging market equities

You Should Know...

While we expect the North American economy to remain healthy, we are cognizant of several factors creating concern about its strength.

The yield curve remains flat to inverted, which often precedes recessions, the ISM Manufacturing Index hit a 2 ½ year low in the U.S. in May, and Purchasing Manager's Index Surveys in the Eurozone and Japan are below 50 - a level that generally indicates a weakening manufacturing sector.

However, we remain optimistic on equities for the following reasons:

1. There are fewer excesses in this economic cycle, which means less need for central banks to tighten, or raise interest rates. For example, U.S. household balance sheets are in good shape after roughly a decade of deleveraging, and capital expenditures have been at modest levels throughout this cycle.
2. The economy is now dominated by services as opposed to manufacturing. Services tend to be less cyclical and do not develop an excess build-up in inventories, which tend to trigger recessions.
3. Labour markets remain on solid footing. Jobless claims remain at very low levels and unemployment is at historic lows.
4. We are in the midst of a technology boom, which should continue to support economic output.
5. Interest rates remain low and have recently declined further, which should support cyclical areas of the economy, like real estate.
6. Equity valuations remain reasonable with forward Price-to-Earnings multiples at relatively attractive levels, by historical comparison, in the U.S. and Canada.

Outlook

Fixed Income

- **MODEST UNDERWEIGHT** domestic government bonds
- **MODEST OVERWEIGHT** high yield bonds and investment-grade corporate bonds
- **NEUTRAL CASH** and inflation-linked bonds
- **MAXIMUM UNDERWEIGHT** global developed market bonds
- **NEUTRAL** global emerging market bonds

You Should Know...

Our overall outlook for bonds remains unchanged from previous quarters. We view the spread of expected returns between equities and fixed income as justification for our overweight stance on equities versus bonds.

We expect coupon-like returns in the low single digits for the foreseeable future, particularly in light of central banks shifting from a tightening stance to a more data dependent approach in determining future rate decisions. We are underweight domestic government bonds due to expectations of muted returns in a prolonged low inflation and interest rate environment.

While economic fundamentals and corporate earnings remain positive, we believe that the themes of slowing global growth, geopolitical events such as BREXIT, global trade tensions, and an inverted yield curve, may lead to greater volatility in the coming months. We remain constructive, and more selective on credit, and comfortable with our modest overweight view on investment grade corporate bonds and high yield bonds, as they continue to offer a yield advantage over government bonds.

Within the global developed bond space, we maintain a maximum underweight view, as low nominal and real yields in Europe and Japan are not compelling.

Canadian/U.S. currency exposure

- **MODEST OVERWEIGHT** the Canadian dollar vs. the U.S. dollar
- **MODEST UNDERWEIGHT** the U.S. dollar

You Should Know...

We maintain a modest underweight on the U.S. dollar (USD).

The potential for slowing U.S. economic growth, coupled with the Fed likely at the end of its tightening cycle for 2019, could put downward pressure on the USD versus a trade-weighted basket of currencies.

We recently moved from neutral to modest overweight the Canadian dollar versus the U.S. dollar. Growth differentials between the U.S. and rest of the world are narrowing and expected to continue. As global growth improves relative to the U.S., demand for the USD will likely wane as it is a counter cyclical currency.

Gold

- **NEUTRAL** gold

We believe an allocation to gold can provide insurance in a portfolio against the risk of extreme outcomes. However, we continue to maintain that this insurance is currently not required.

TD Wealth Asset Allocation Committee

The TD Wealth Asset Allocation Committee (WAAC) was established to deliver a consistent asset allocation message and be the source for active asset allocation advice across TD Wealth.

The committee has three prime objectives:

1. Articulate broad market themes
2. Provide macro-level asset allocation
3. Identify the major risks on the horizon

Committee Members

Chair: Bruce Cooper, CFA
CEO & CIO, TD Asset Management Inc. and SVP, TD Bank Group

Michael Craig, CFA
Managing Director,
TD Asset Management Inc.

David Sykes, CFA
Managing Director,
TD Asset Management Inc.

Robert Pemberton, CFA
Managing Director,
TD Asset Management Inc.

Glenn Davis, CFA
Managing Director, TDAM USA

Kevin Hebner, PhD
Managing Director,
Epoch Investment Partners, Inc.

Brad Simpson, CIM, FCSI
Chief Wealth Strategist, TD Wealth

Sid Vaidya, CFA, CAIA
U.S. Wealth Investment Strategist,
TD Wealth

Bryan Lee, CFA
Vice President & Director,
TD Asset Management Inc.

[1]Sources: www.td.com/document/PDF/investor/2019/2019-Q2_Financial_SuppPack_F_EN.pdf
www.rbc.com/investorrelations/pdf/19q2supp.pdf., https://www.bmo.com/ir/qtrinfo/1/2019-q2/Suppq219.pdf
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