



View from the Top

Monthly Perspectives
September 2024

15 minutes

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Beata Caranci, Chief Economist | TD Economics

Brad Simpson, Chief Wealth Strategist | TD Wealth

David Sykes, Chief Investment Officer | TD Asset Management | TD Wealth

Every year around this time, the Wealth Investment Office reaches out to TD's "Three Chiefs" of the financial world: Chief Economist Beata Caranci, Chief Wealth Strategist Brad Simpson and Chief Investment Officer David Sykes. Together, they offer an invaluable pool of insights that help to frame the economy, the markets and where we go from here as investors.

This year, our panel discussion wandered into some challenging territory — historic volatility, momentous elections, even the threat of global warfare — but our luminary triumvirate didn't flinch, shedding light on trends and themes that cut through the market noise.

■ **WIO:** Let's start with the recent spike in volatility. The VIX had been at historic lows, trading between 10 and 20 for the whole year, and then over just a couple of days starting at the end of July — after the Bank of Japan said it was going to continue to raise rates — it spiked to 60, and the Nikkei fell 12% in a single day. David, let's start with you. Is this volatility something we should be concerned about?

Sykes: I think the answer to that question is, it all depends. It depends on whether that spike was a sign of economic deterioration, like you saw in the global financial crisis, or was it a sign of extreme market valuation? I don't think that was the case this time around. Really, in this situation, it was this technical unwinding of levered carry trades that were using cheap yen financing. If it had been because of a slowing global economy or really high valuations, then I think that would have given us more pause, but I think, in this case, the reason the VIX spiked was this technical leverage situation.

■ **WIO:** Right. Traders borrowing yen because of Japan's super-low interest rates. And then the Bank of Japan caught these levered traders off guard. I suppose it doesn't help that the Fed insists on being "data-dependent" and refuses to commit to policy over the long term.

Sykes: Actually, it's the opposite. If anything, they're being very pragmatic with that flexible, nimble, data-dependent approach. I believe that data dependency actually lowers volatility over time. If you think about the period we've just come through, we're going through major demographic changes in the economy. Labour shortages, supply-chain imbalances — this is truly a novel economic cycle, augmented by Covid — and I think by being data-dependent and willing to adjust, it shows that the central bank is being humble and is ready to adjust in a rapidly changing environment. And I think the market actually agrees with us, because if you look at the VIX today, we're back down to 16 or 17, which is below the 10-year average of 18.

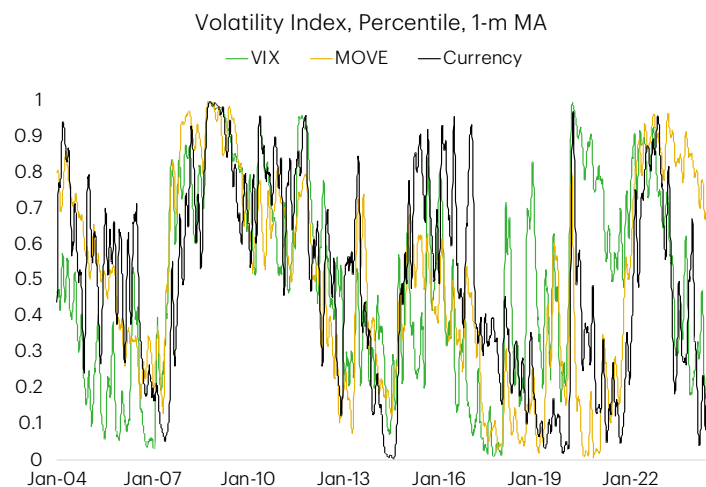
■ **WIO:** Brad, volatility is something that you and your team have written a lot about in the past few months. How should clients be thinking about it?

Simpson: In our last *Portfolio Strategy Quarterly* [Q3 2024, "All is Quiet?"], which interestingly was published on July 30, we drew attention to the oddly calm environment that existed through the first half of the year. It was particularly interesting given the environment — unusually high concentration in equity markets, heightened geopolitical tensions and the shifting regime of central banks. The implied correlation among stocks within the S&P 500 had fallen to its lowest level since the inception of the VIX in 1993, which was a result of the bifurcated market where highly valued big tech names moved inversely to the rest of the market (Figure 1).

PSQ: All is Quiet ([Click to open](#))



Figure 1: Volatility Spikes



Source: Macrobond, Wealth Investment Office, as of September 8, 2024

We were concerned that markets were too complacent given the backdrop, and that certainly played out during that first week of August. It's not just equity volatility, either. Volatility has picked up in bond and currency markets as well. While some investors take this as a real negative, we view it as a positive. We are of the view that this is more likely a step towards a new normal in terms of volatility, rather than a sign of significant deterioration of financial markets. In terms of the macro outlook, the consensus continues to believe that a soft landing is the most likely scenario, which we tend to agree with. But it's also important to emphasize that equity, bond and currency volatility isn't all bad; it can create some attractive opportunities for investors.

■ **WIO:** Okay, let's look at some of the data that's leading the Fed. Inflation, for instance — is the disinflationary trend around the world going according to plan? Beata, I believe this one's in your wheelhouse.

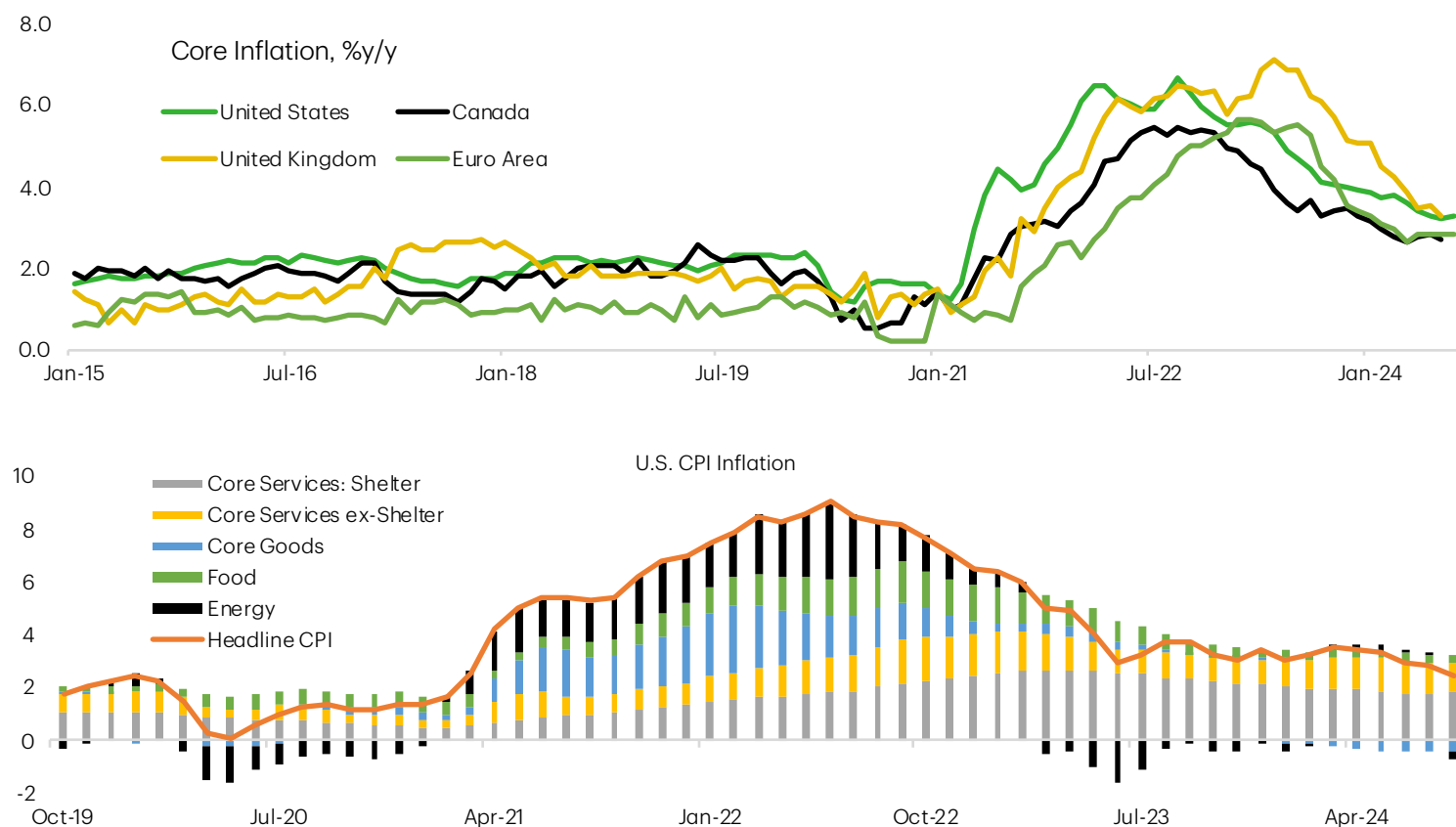
Caranci: Certainly. For the major central banks looking to tame inflation — the European Central Bank, Federal Reserve, Bank of Canada and Bank of England — price pressures are now cooling largely in line with expectations. More importantly, the declines are not solely driven by food and energy prices. Central banks are comforted by the share of categories with prices running above 3% year-on-year, which has stepped down significantly in the past year.

However, the road ahead might be bumpy given that prices for services have shown persistence. The downdraft on inflation has come mostly from weaker prices for “stuff,” or from the goods sector. In contrast, service prices are still too elevated. Removing shelter costs to get like-for-like measures across countries, service inflation is running at nearly 5% in the U.S., and even hotter in the UK at 6%. The euro area and Canada are the best performers, and yet both are holding at a still hefty 4%. Fortunately, the U.S. has shown a notable improvement in the near-term trend, where the three-month annualized change has ticked down to 3%. In all other jurisdictions, it's gone the other way, but this merely reinforces how tenuous the environment remains because the exact opposite story played out last quarter.

■ **WIO:** So service inflation remains high, but clearly the Fed has already begun its easing cycle. Do you think it's likely to cut rates rapidly or take its time?

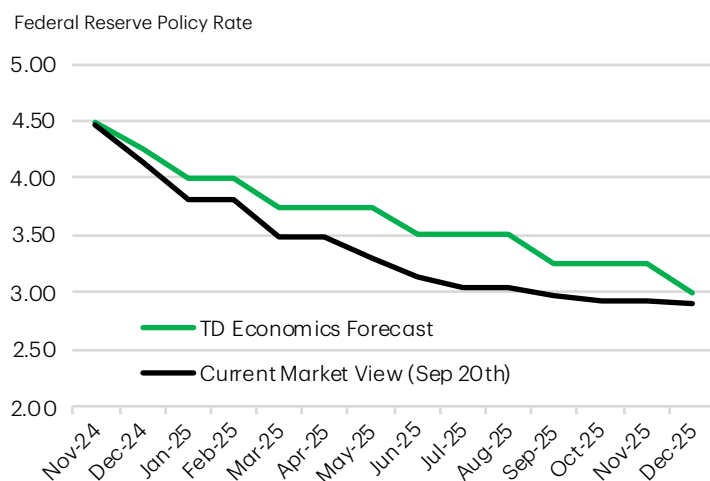
Caranci: Markets are signalling that the Fed is starting on its back foot, since it's the last central bank to come off the sidelines, and it has the highest policy rate. The fact that labour demand is slowing reinforces that the Federal Reserve can't wait for all the stars to align on inflation, or it risks having to cut more aggressively if too much slack builds in the economy.

Figure 2: The global disinflationary trend continues apace



From our perspective, the economic slowdown is not a reason for panic. It's a necessary condition for the Federal Reserve to build confidence that inflation will remain under control, even though it hasn't come in for a perfect landing yet. We anticipate the Fed will lower the policy rate down to 4.25% by the end of 2024 and move it towards 3.25% by the end of 2025 (Figure 3).

Figure 3: Policy-rate expectations are coming down for 2024



Source: Bloomberg Finance L.P., TD Economics

We have greater certainty on the outlook for the pace of rate cuts for the Bank of Canada, given that it has already established a trend in recent months. The policy rate is already 75 basis points below its U.S. counterpart, and the Bank of Canada has set a precedent of cutting rates by 25 basis points in each of the past three meetings. This creates a higher bar to alter the course. We expect that the BoC will deliver a quarter-point cut at each of its next two announcements. This will bring the policy rate to 3.75% by year end — a significant amount of easing from the 5.0% level just a few months ago. If the economy sticks its soft landing, that would give the central bank room to return the policy rate to 2.50% by the end of 2025, so long as the housing market doesn't catch fire again.

■ **WIO:** If we go back to volatility and think about currency volatility, it leads us to the U.S. dollar. If the Fed were to cut faster than its peers, would that weigh on the U.S. dollar? We've already seen a weakening, particularly against the yen and euro.

Caranci: The U.S. dollar was on an incredible run over the first half of 2024. It's up around 5% on a trade-weighted basis. The relative strength in economic performance caused markets to anticipate a widening in spreads to peer countries, which proved correct until July. The recent Fed pivot has caused the U.S. dollar to depreciate just over 3% since the start of July. Much of this has been against the yen, which has climbed approximately 11% over that time. The Bank of Japan is embarking on the opposite interest-rate cycle, with hikes, and that has unwound some of the carry trade. But many

other currencies have also been caught in the upswing, like the euro, the Swiss franc and Singapore dollar.

As for Canada, the loonie has largely traded sideways to the U.S. dollar while depreciating against peers. This partly reflects the offsetting impact of falling energy prices. This lack of direction for the loonie is expected to persist going forward, with offsetting influences keeping the currency within its current 72-to-76 U.S. cent range.

We always caution on perceiving the greenback as a one-sided risk, though. It could well be in for a reversal later this year if market focus shifts back to geopolitical factors and a flight-to-safety trade kicks back in, which benefits the U.S. dollar. One such event can come from the U.S. election. Does it open the door to a rehashing of trade disputes, or tax cuts, or greater uncertainty for America's peers? Any one of these can drive investors to seek the shelter of King Dollar once again.

■ **WIO:** What about from a market perspective? David, if the U.S. dollar continues to weaken over the next six months or so, will that put pressure on U.S. equities, or is it still too early to start increasing allocation to international and emerging-market equities?

Sykes: I don't think it's the beginning of a longer secular trend, because if you're going to make the case that the U.S. dollar is going to be weaker on a longer-term basis, I think what you're saying is that economic growth in the U.S. versus the rest of the world is going to slow sharply — and I don't believe that. I still think the United States is going to have above-trend growth versus the rest of the world. We still view the United States economy as more innovative and faster-growing relative to Europe and relative to Japan. We don't think this is going to cause a longer-term devaluation of the U.S. dollar.

■ **WIO:** Brad, how do you think about the U.S. macro backdrop, relative to the rest of the world when you are allocating assets?

Simpson: We also believe that it's difficult to see how the U.S. economy falters in any meaningful way relative to other regions for any extended period of time. While we are seeing some of that U.S. exceptionalism fade with recent economic data, we agree with David and Beata that the U.S. economy is likely going to continue to deliver above-trend economic growth. While growth is slowing in the U.S., the macro landscape outside the U.S. is also slowing, and those regions are from a weaker starting point.

We've spoken many times about how the world has decoupled and we are seeing different cycles and different stages in different countries. China is early-stage, while Japan, Europe, Canada and the U.S. appear to be late-stage. But the U.S. economy is definitely the elephant in the room. The second player is China, and it's facing some significant structural challenges. So we are very focused on the U.S., and have been for some time now.

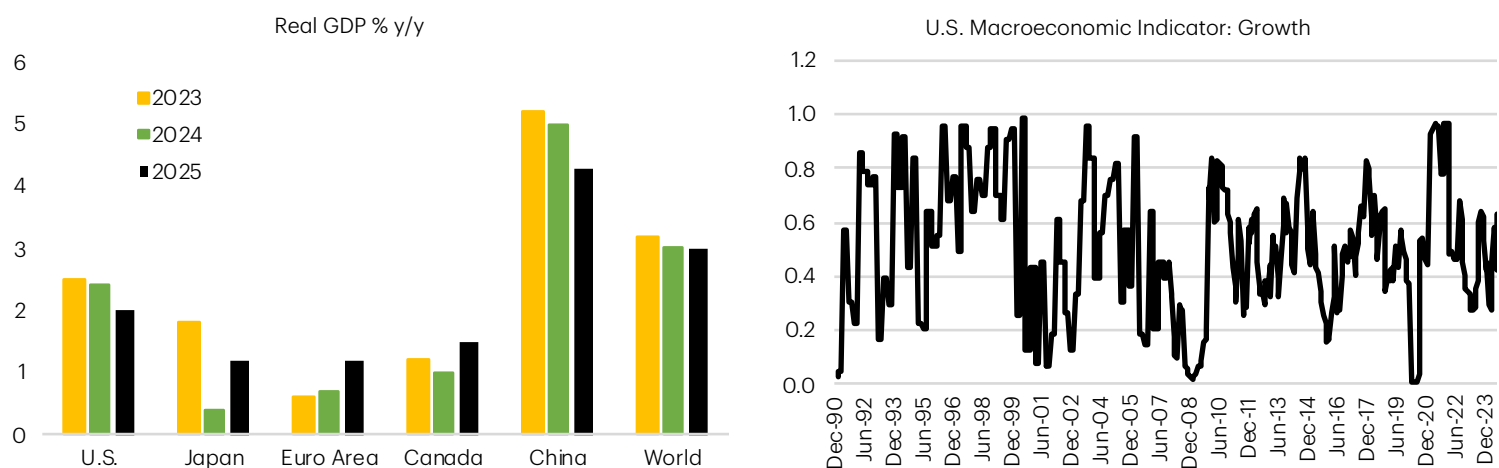
On the growth front, U.S. economic growth has moved to the 63rd percentile of its 30-year historical range today, an improvement when compared to a year ago, when it was in the 38th percentile. This highlights that U.S. real economic growth remains healthy.

In the U.S., we are focused on labour markets. In August we saw the increased volatility and correction on a weak employment print. Really, the market was waiting to trip on something, but a soft landing will definitely hinge on employment because having a job determines whether or not you keep spending. We know employment has weakened in the past two years, but on an absolute basis, it's still a positive story. The consumer story is similar. Yes, it's been weakening since 2022 but it's still holding on very well. This is the key for us right now, and we are watching the changing rate of growth closely. For now, we're still of the view that a soft landing is likely.

The story in the consumer sector is one of a convergence between spending intention and actual spending. Consumer sentiment has been and is still depressed. However, retail and personal spending have fallen further below the historical average. Other than the employment category, this is the segment worth monitoring closely because a soft landing requires both categories to stop decelerating sharply from current levels.

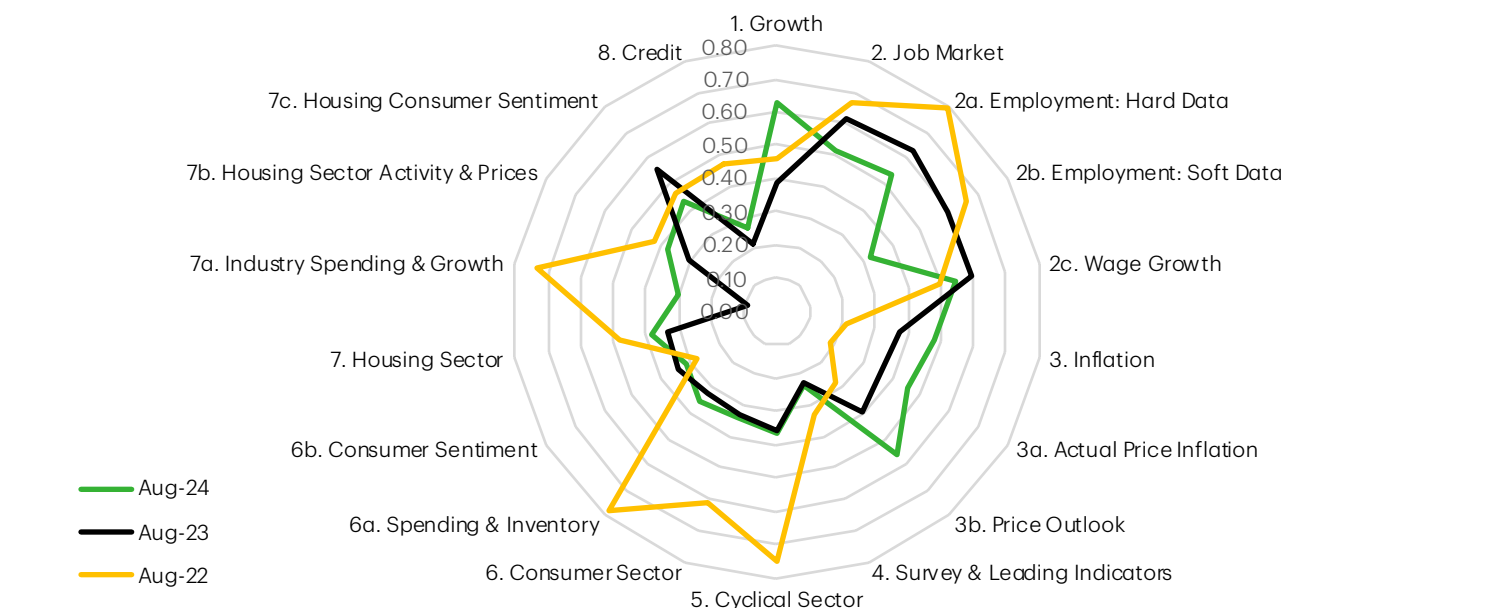
One notable improvement is on inflation, as measured by both actual price inflation and price outlook. Although actual price inflation remains too high — it's slightly below the 50th percentile — its outlook has improved significantly to the 56th percentile from the 28th percentile two years ago. This corroborates Chairman Powell's speech at Jackson Hole, which noted that "confidence has grown that inflation is on a sustainable path back to 2%."

Figure 4: U.S. economy continues to outpace peers in developed regions



Source: TD Economics, IMF and Wealth Investment Office as of September 2024

Figure 5: U.S. Macroeconomic Indicators



Source: Macrobond and Wealth Investment Office as of September 12, 2024

The bottom line is that we are still in the late stage of the U.S. business cycle, where cyclical and housing-sector activity are potentially getting close to a bottom and would benefit from the tailwind of monetary-policy easing. Inflation continues to improve, and the softening trajectory in the U.S. labour market is concerning but is not yet a red flag.

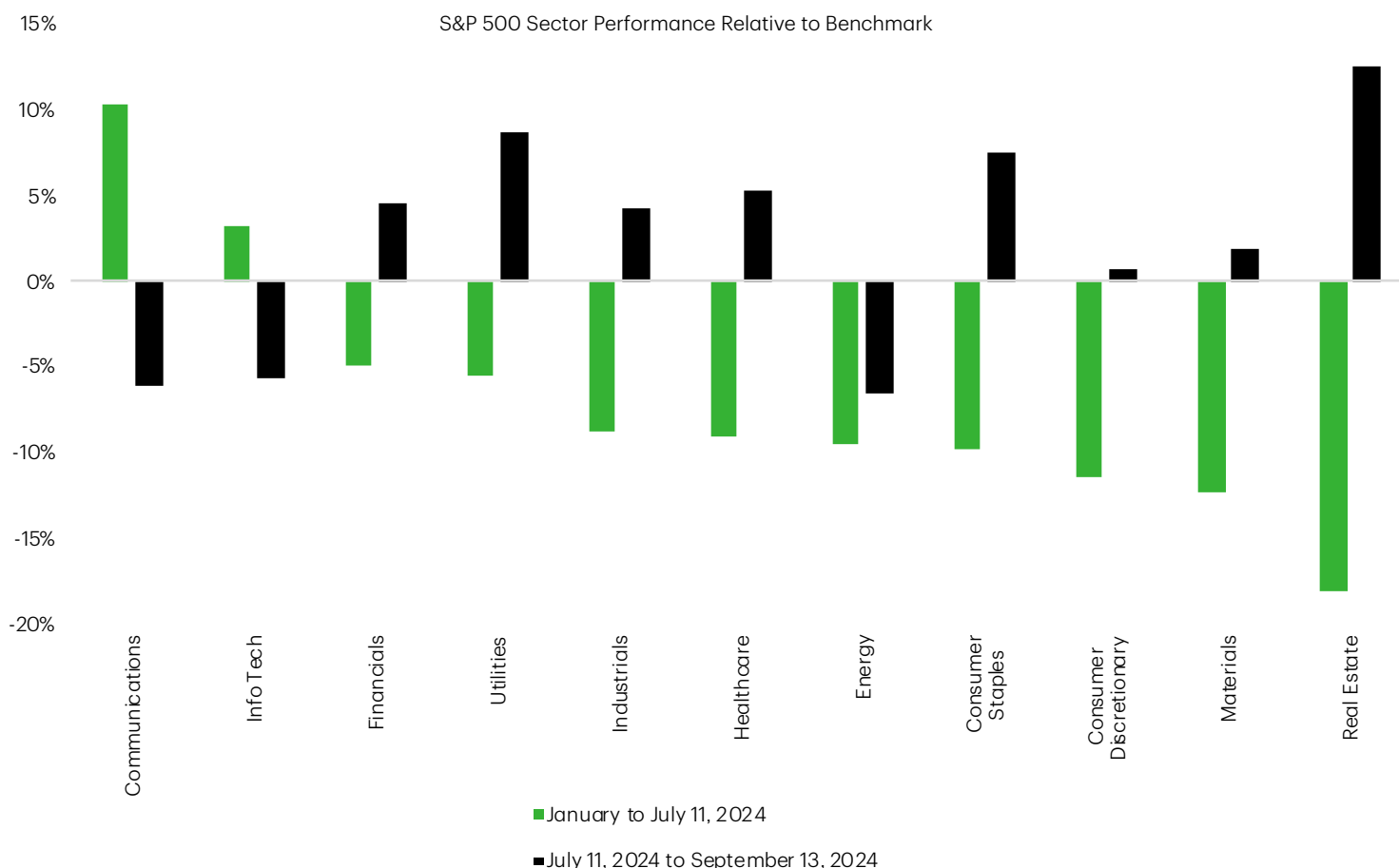
When we look at our recommended allocations across equity markets, we continue to hold an overweight position in the U.S., and market-weight or underweight positions in all other regions. While valuation levels are relatively attractive in other regions, the headwinds facing those regions remain elevated. We have maintained this overweight U.S. position for the last year, and the U.S. has consistently delivered relatively solid economic data.

■ **WIO:** American markets are starting to look stretched, though, particularly the big tech names. Is now a time to be defensive, or is it just a matter of riding out any volatility and moving into areas of relative value? David, maybe you can answer?

Sykes: Sure. So, I think that plays a little bit into the volatility theme that you started with. If we look at the S&P 500 today, we're at an all-time high. And so I think it's fair to say that people are cautious, people are nervous — they're waiting for the next shoe to drop, which may be why cash levels still appear to be elevated among retail investors.

However, since the middle of July, when U.S. inflation came out relatively tame, you started to see the market broaden out beyond big tech, and you started to see interest-sensitive stocks like financials, like utilities, like real estate start to do well. If inflation stays tame and the Fed continues to cut as we go through '24 and '25, I think that gives us more confidence that the market is not going to be experiencing a significant hard landing or a large drawdown.

Figure 6: Sector Rotation



■ **WIO:** Brad, what's your take?

Simpson: Cash levels are still elevated, telling us that, on one hand, investors are cautious, while at the same time valuations in many names are elevated, which suggests investors are bullish. It's an interesting mixed message. Many of our portfolios have taken a barbell approach, where we have exposure to quality tech names that we believe are more fairly valued on the growth end and quality defensive positions, such as health care and consumer staples, at the other end. With some of our recent portfolio adjustments, we are also well positioned for a market rotation, increasing our exposure to quality defensive sectors while also maintaining exposure to cyclical sectors such as industrials and energy.

■ **WIO:** Does this kind of bifurcated equity market — where you have to choose between expensive tech stocks and low-growth stocks elsewhere — does it pose an allocation challenge for fund managers like yourself, David?

Sykes: Currently we're trading around 21 times forward earnings for 2025. It's fair to say that, historically, that's an elevated level. But it's also fair to say that the market composition has changed significantly. The market used to be about energy and financials, which typically had much lower P/E multiples. But the composition of today's market, it's really driven by businesses with low capital intensity. They've got very high margins, and they have very high and sustainable free cash flow and low debt. I think that does support a higher multiple. While you never want to overpay, and you always want to keep an eye on valuation, from our standpoint, I think there are a number of secular trends and quality compounders, and we continue to see lots of opportunity there.

■ **WIO:** What about you, Brad? Is it hard to allocate in this kind of market?

Simpson: To broaden out from David's point, an area we think warrants attention is the private-asset space, which offers many interesting alternatives for investors today. Public markets are often impacted by noise, which can cause major distortions in investment returns. In addition, with the growth of algorithmic trading systems and quantitative investing in public markets, underlying fundamentals can get frayed in the short term by speculators. For investors who are truly interested in owning the company, versus the stock, private assets offer compelling opportunities. In private markets you are always an active investor. The LPs or GPs can implement changes and make active decisions with a management team that is aligned with investors' best interests. With the growth in private-asset alternatives, many companies are staying private for longer, which has resulted in attractive opportunities for private-asset investors.

What's more, when we look at direct lending, a firm can be flexible in customizing terms so that they can fund businesses or companies that may not fit well into the standard covenants. Just like public investments, the underlying asset

and management teams are key, but truly skillful lenders can shape the bilateral deal and seek the best risk/return characteristics.

■ **WIO:** Very interesting. Let's talk about some emerging themes that may not have gotten enough attention. David, maybe you can address the public markets, and then I can ask the same question of Brad for private markets.

Sykes: Sure, no problem. I think the performance of the cyclical sectors has been overlooked. Brad spoke earlier about having exposure to cyclicals such as industrials, which we agree with. There's been a lot of talk about the Mag7 and artificial intelligence, but if you look inside the industrial sector, we've seen some stocks that have really benefited from secular trends like infrastructure spending, which obviously is driven by the AI boom. If you look at on-shoring or re-shoring, you're definitely seeing some industrial stocks benefit. Also, themes around electrification and decarbonization.

■ **WIO:** And in the private market, Brad?

Simpson: When we think about that very popular theme of AI, we have a public-market champion today with many sizeable players. They operate in the bits or digital world of software. However, to make the technology a reality in everyone's daily lives, we have to care about hardware and the physical world we live in. Sequoia estimated it needs capex equal to the amount invested in the software space — currently, at \$200 billion a year — to be deployed into physical investments to house the hyper-scaler's data centres. This is happening much slower and is increasingly supported by private capital. We just saw the buyout of AirTrunk, a major data-centre player in the Asia Pacific region. The buyers include Blackstone and CPPIB. The rationale is, by plugging into the vast amount of private capital, quality business operators can deliver a project more quickly.

In health care, one of our colleagues at TD Securities Cowen mentioned in a recent interview that biotech firms today can stay private longer if they are developing a technology that is truly game-changing. There are large pools of capital that are specifically deployed in this area to facilitate medical advancement. It's very exciting.

■ **WIO:** Are you also looking at companies such as industrial REITs and data centres in the public markets?

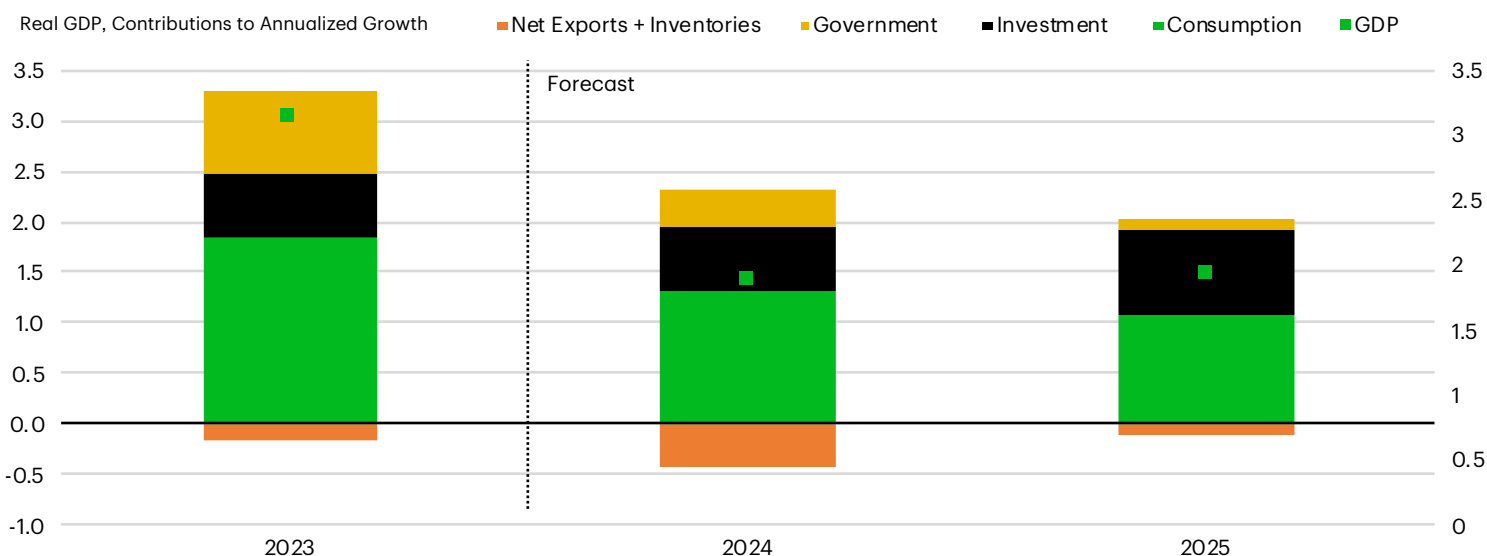
Sykes: For sure. The data centre interest is there, but again, valuations are very lofty in that space because a lot of folks already know about that. When you're trying to find the hidden value, you have to start thinking about the components from industrial companies that have to go into data centres — all of the materials and the elements and the coordination and the software that an industrial company has to employ to build that data centre. To get the temperature just right. To make sure that those data centres are located in the right place, with the right humidity. That's what we're talking about when we talk about that industrial theme.

■ **WIO:** Thanks, David. Let's change gears somewhat. Another source of volatility is the upcoming U.S. election, which inevitably brings out some fearmongering as the candidates issue dire warnings about what might happen to the economy if their opponent is elected. Beata, is there any merit to some of these warnings, particularly given the weakening of the U.S. labour market?

Caranci: Markets are not completely in left field to worry about the downshift in U.S. momentum, but nothing in the data foretells a stalling out at this point. So far, the data reinforce an expansion that has downshifted from fourth gear into second. The 4% annualized expansion through the second half of last year has decelerated to a trend-like pace of 2% in the first half of 2024 (Figure 7). However, this shouldn't be interpreted as bad news. It provides validation that the "long and variable lags" of restrictive monetary policy are finally starting to tighten their grip on the economy — a necessary condition to wring out the last bit of inflationary pressure and open the door for more interest-rate cuts.

Nearly half of the slowdown is attributed to cooler consumer spending, which shouldn't come as a surprise. Some warning flares have been shot up, but this has to do with the high level of interest rates, and not who becomes the next president and their policies. The tailwind from excess savings has been exhausted, leading consumers to increasingly rely on debt to fund spending. In non-mortgage products, the upward migration in delinquency rates has now exceeded pre-pandemic levels. To give an idea of the interest-rate burden, the share of income that households are dedicating to servicing non-mortgage debt is closing in on levels last seen during the 2008 financial crisis. This is a clear case for the central bank to get going on lowering its policy rate as the job market cools in parallel.

Figure 7: The U.S. economy is downshifting

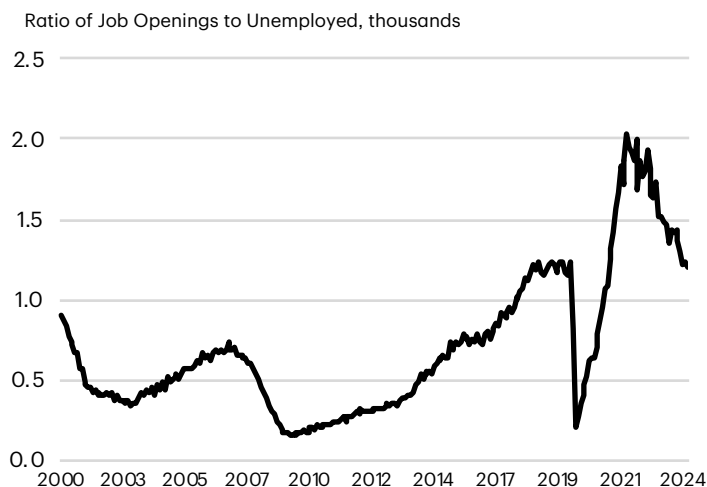


Source: Bureau of Economic Analysis, TD Economics

The U.S. unemployment rate has risen through the first seven months to 4.2%, a near three-year high. So far, the rise has been highly influenced by an increase in people entering the labour force compared to job losses and temporary layoffs. That gives the Fed time, but not a pass. They must be careful when it comes to firm behaviours where inertia can build on hiring, making it difficult to influence once a downtrend is established.

The bottom line is that the U.S. economy is slowing, but not buckling. Investors are adjusting to the realities of this new paradigm after last year's breakneck pace (Figure 8). It's uncertain what the U.S. election will bring from a policy perspective, but the main catalyst to whether the U.S. ultimately enters a recession is more likely to stem from whether the central bank has it right on the timing and scope of interest-rate cuts. For now, the person who wins the White House in November is likely to inherit a resilient economy.

Figure 8: Labour-market imbalances are quickly normalizing



Source: Bureau of Labor Statistics, TD Economics

■ **WIO:** What about you, Brad? Do you think this election will have a major impact on markets?

Simpson: So we think about this from a different angle. There is the economic impact of this, which Beata is watching closely, but the immediate market impact is often something else, which is something that David and I watch closely. I think we have to be careful with how we think about the impact of this election. U.S. elections happen every four years, and every time experts come out and pontificate on scenario analysis. If the Republicans win, markets look like this, and if Democrats win, markets look like this.

This time, it's a very different type of election and a very different environment that we find ourselves in. You don't know if one side will accept the result, you don't know if one side will respect the Constitution and the rule of law. That rule of law is what makes U.S. capital markets the most trusted in the world and the greenback the world's reserve currency. So if that is questioned, it opens up an unknown outcome.

What we need to learn from 2016 is that we didn't know who was going to win. None of us knew. Initially markets fell, but then rose as areas of the market benefitted from the election of President Trump. Here at TD Wealth, we went overweight U.S. markets shortly following that election.

We believe in adaptive markets, and we will make the decision on how to allocate the day after this election, once the results are known. We think the best way to manage for this election is to stick to your process, adapt to what's in front of you, and make sure you own a well-diversified investment portfolio. We do expect to see ongoing spikes in volatility, though, over the next few months.

■ **WIO:** So, neither candidate is going to singlehandedly drag the U.S. into recession. But there are still some pretty big differences between their platforms. David, let me ask you, if the Democrats can pull off a victory, will that deflate some investor hopes for another Trump-style tax cut, particularly given Harris's proposal to raise the U.S. corporate tax rate?

Sykes: There's no question that the markets would love to see lower tax rates at the corporate level. I do think the market is going to be really, really fixated on exactly what you said. It's around taxation, but it's also going to be around regulation, immigration and tariffs. Those are the big, big policies. But I would also just caution people, it's not just the presidential race that matters, it's also going to be the composition of Congress. So, who wins the House, who wins the Senate is going to be very important. Election campaigns are all about the politics of the possible, but if you get ownership of the Oval Office, but Congress is controlled by the other party, it quickly becomes politics of the impossible. And so we'll have to wait and see how this goes. Overall, though, the premise is correct — if you saw an extension of existing corporate tax relief or additional corporate tax relief, I think that'd be very positively viewed by the market.

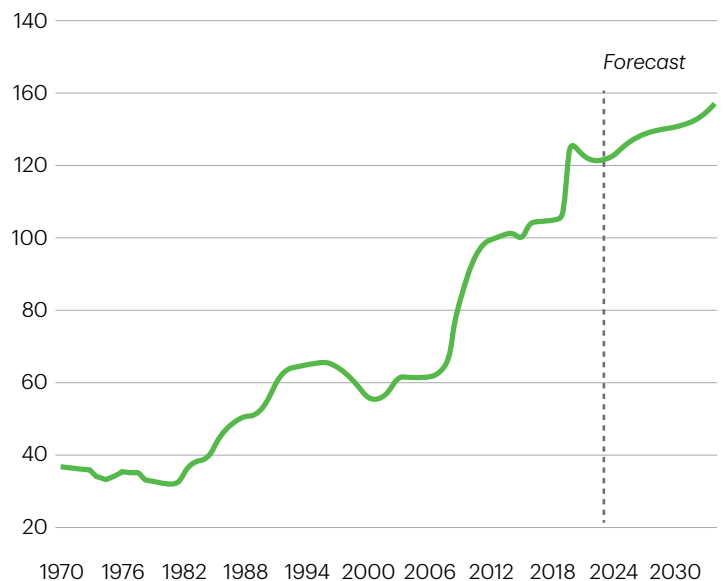
■ **WIO:** Over the long term, though, big tax cuts and big spending programs increase deficits. Biden and Trump were both viewed as populists, and neither seemed particularly interested in bringing down deficits. Which of the current candidates do you think would be more fiscally prudent?

Sykes: I don't believe the market views either candidate as good for the U.S. debt or deficit. I think that's been very clear. We haven't seen a lot of detail regarding Harris's policies as of yet, so this could change. It's something we're watching closely. Overall, if you look at the United States today, the deficit as a percentage of GDP is somewhere in the 5% to 7% range — that is very, very high, particularly with unemployment as low as it's been.

I think one longer-term worry I have is that, if Trump or Harris are successful with the things they are talking about, the deficit as a percentage of GDP will only rise, and the debt burden as a percentage of GDP will only rise. If that happens, you're going to find yourself in a situation, in one, two, three, four years, where the term premium for longer-term Treasuries is going to have to rise because you could easily see yourself at 120%, 130% debt-to-GDP. And neither candidate has talked about fiscal prudence and getting that under control.

Because of where interest rates are today and because of tax cuts and because of massive fiscal programs, right now in the United States, they're spending just as much on interest to service the debt as they are on defence. And so there are a lot of implications from this. The market doesn't seem to be focused on it in the short term, but my hunch would be in two, three, four years, this will become a very important issue.

Figure 9: U.S. debt-to-GDP has skyrocketed



Source: Congressional Budget Office, TD Economics

■ **WIO:** Brad, what do you think?

Simpson: U.S. politics remain a circus, although Harris's approach, at least in the first debate on September 10, appears to be to try to shift away from that circus and move towards a more professional stance. At this stage we still do not know very much about either candidate's policy plans. At the same time, regardless of who wins the presidency, the makeup of Congress and the Senate will be key. Most important for clients is to stick to your process, stay diversified, both in terms of asset allocation and global diversification, and adapt to the environment around you. That is always the best course of action and will allow you to achieve your long-term goals without being pushed off track by the circus noise.

■ **WIO:** I suppose there's also risk from a trade perspective, particularly if Trump wins a second term. He and Biden were both protectionists, but Trump's plan for a second term seems even more so. Beata, what would you say is the risk to international trade posed by the U.S. election?

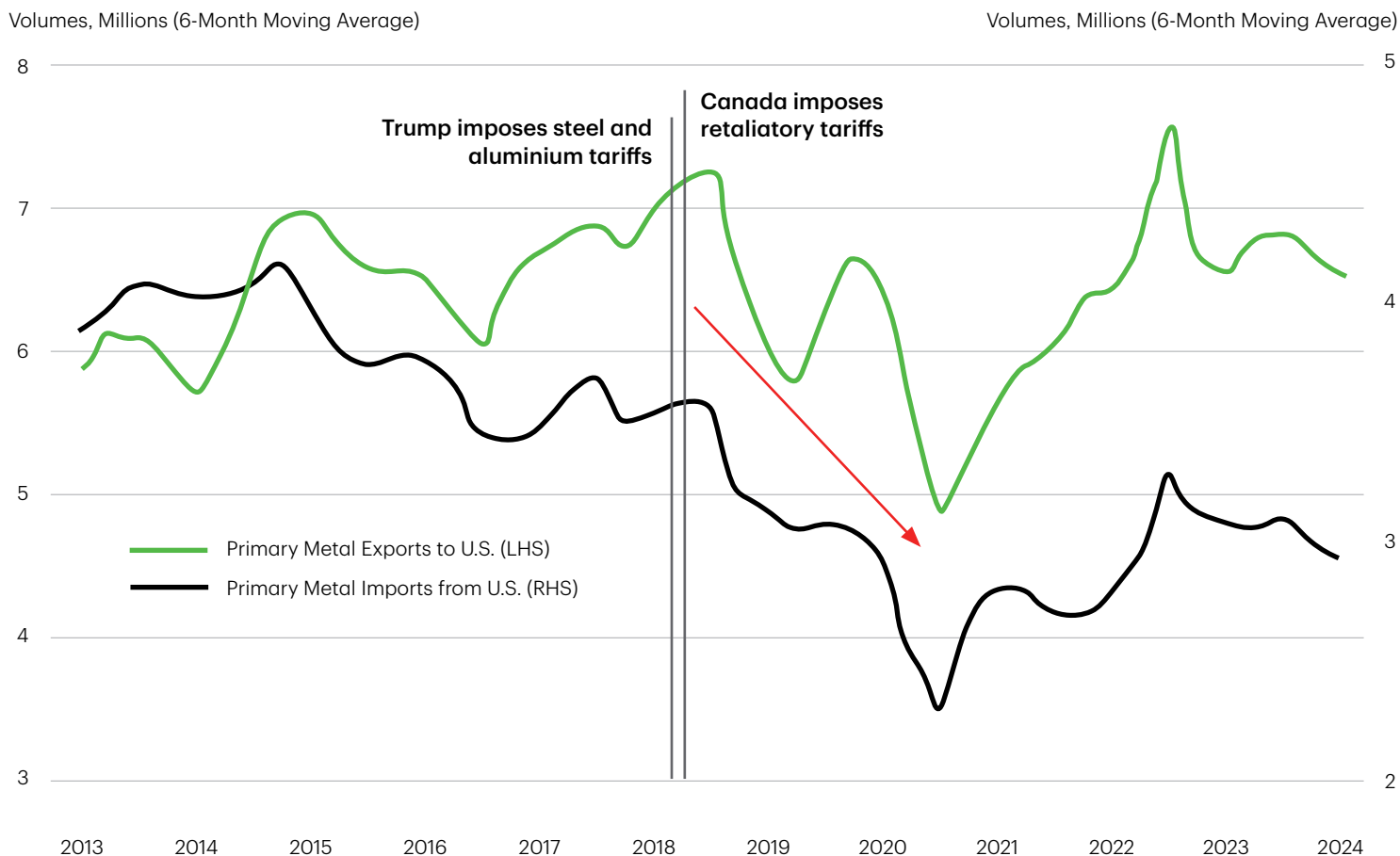
Caranci: Regardless of who wins in November, global trade will have to contend with an America that's leaning into industrial policy and self-reliance. The key differentiator will be whether the new administration decides to "go it alone" or works with allies on strategic sourcing initiatives. A Trump

administration is a bigger risk for Canadian trade flows given blanket statements on 10% tariffs and interest in revisiting the USMCA when it comes up for review in July 2026 — albeit a Harris administration would also likely seek some alterations.

Estimates on economic impacts are always going to be dire when there are sudden and large tariff impositions, but there is a precedent to check on this logic and the magnitude of effects. Trump's prior tariffs on Canada were on strategic items, like lumber, steel and aluminum. They didn't have the scale to seriously undermine total trade but did negatively affect the targeted sectors.

Trump's marquee tariffs on Canada, for instance, were 25% on steel and 10% on aluminum, which were maintained for one year. During this time, Canada imposed a retaliatory tariff on U.S. steel and aluminum imports. Import and export volumes both moved immediately lower (Figure 10). A rebound didn't occur until the tariffs were lifted, which was subsequently interrupted by the pandemic. Now imagine if Trump becomes president and enacts far-reaching or indiscriminate tariffs. You could see this negative outcome repeated across all the impacted sectors. It's reasonable to expect a substantial hit to market sentiment.

Figure 10: Impact of 2018 Tariffs



Source: Statistics Canada, TD Economics as of Q1 2024

■ **WIO:** Of course, aside from the trade wars, we also have real wars to contend with. We've already got wars in Ukraine and Gaza, and threats abound. Have the wars so far had much of an impact on market performance?

Sykes: There's been a massive human toll, and the tragedies that unfold are very hard to watch, but from a market perspective, no, there hasn't been nearly the impact that the market had feared. In the Russia-Ukraine situation, you have seen increased energy costs for Europe, but overall, the impact for markets has been relatively small. With the conflict in the Middle East, there's always concern and worry, but there really haven't been any major market implications. I've been very surprised that it hasn't had a bigger impact, but if we think about a scenario where this escalates to a NATO-level engagement or a wider regional war in the Middle East where Lebanon and Iran are involved, I think that would be a huge concern for the market. We just have to hope and pray that that doesn't happen, but if it did, I think that would be a market-moving event and one that would be very concerning from a stability standpoint.

■ **WIO:** Brad?

Simpson: Sadly, global geopolitical risk has been elevated for some time now and, as David said, the tragedies are difficult to watch. In terms of market impact, we often see an immediate market reaction, but the medium- and longer-term impacts tend to be less. We are mindful that the tensions in the Middle East add to risk in energy markets. Also looming in the background is the threat of a larger escalation between the U.S. and China, and the potential impacts.

When we think about volatility, we often think of the downside risk, but that is not the only aspect. Volatility to a strategist is what earnings are to an equity analyst. Equities, bonds and currencies have seen higher volatility. All have been increasing, and for us this comes back to how we allocate. We think that we are in an environment where we get these major spikes in volatility.

Between election risk, geopolitical risk, economic uncertainty across the world, equity valuations and the significance of tech, we think volatility was ready to spike in August. This is something that we have been writing about for the past few months. We have also been implementing various strategies. For instance, for equities, we have been implementing hedging strategies and options strategies in our diversified mandates in order to mitigate the risk of volatility spikes in equity markets. With volatility so low for much of the year, we've seen very attractive opportunities to implement those strategies.

If we look at bond markets, we have seen elevated volatility for the past two years, and there we have added solutions that are designed to minimize the negative impact of interest-rate volatility in that market. In general, investors hear the word

volatility and believe it means losses. However, it's important to understand that volatility creates tremendous opportunities for active management and to capture alpha — to enhance risk-adjusted returns.

Successfully navigating this regime will require a nimble approach and flexible framework capable of adjusting on the fly as the economy reacts to yet unknown policy changes and unexpected shocks.

■ **WIO:** Thanks so much, Brad. I think we'll leave it there. This has been a fascinating discussion. We greatly appreciate all of your insights, and it was a pleasure speaking to you all.

Simpson: The pleasure's all mine. Looking forward to revisiting this all again next year.

Caranci: Many thanks.

Sykes: Thanks, everyone.

Market Performance

| | | (%) | (%) | (%) | (%) | (%) | (%) | (%) | (%) |
|--|--------------|-----------------|-----------------|----------------|-----------------|------------------|------------------|-------------------|-----------------|
| Canadian Indices (\$CA) Return | Index | 1 Month | 3 Months | YTD | 1 Year | 3 Years | 5 Years | 10 Years | 20 Years |
| S&P/TSX Composite (TR) | 95,511 | 1.22 | 5.65 | 13.65 | 18.77 | 7.58 | 10.63 | 7.32 | 8.32 |
| S&P/TSX Composite (PR) | 23,346 | 1.02 | 4.84 | 11.39 | 15.05 | 4.29 | 7.26 | 4.10 | 5.26 |
| S&P/TSX 60 (TR) | 4,683 | 1.67 | 5.97 | 13.16 | 19.14 | 7.87 | 10.91 | 7.90 | 8.72 |
| S&P/TSX SmallCap (TR) | 1,440 | -1.26 | 2.46 | 13.70 | 14.18 | 3.61 | 8.66 | 3.58 | 4.63 |
| S&P/TSX Preferred Share(TR) | 2027 | 2.71 | 4.99 | 19.92 | 30.50 | 2.17 | 7.19 | 2.68 | 2.95 |
| U.S. Indices (\$US) Return | | | | | | | | | |
| S&P 500 (TR) | 12,344 | 2.43 | 7.39 | 19.53 | 27.14 | 9.38 | 15.92 | 12.98 | 10.65 |
| S&P 500 (PR) | 5,648 | 2.28 | 7.03 | 18.42 | 25.31 | 7.69 | 14.06 | 10.92 | 8.50 |
| Dow Jones Industrial (PR) | 41,563 | 1.76 | 7.44 | 10.28 | 19.70 | 5.53 | 9.50 | 9.29 | 7.29 |
| NASDAQ Composite (PR) | 17,714 | 0.65 | 5.85 | 18.00 | 26.21 | 5.10 | 17.34 | 14.48 | 11.99 |
| Russell 2000 (TR) | 11,936 | -1.49 | 7.51 | 10.39 | 18.47 | 0.60 | 9.68 | 8.03 | 8.70 |
| U.S. Indices (\$CA) Return | | | | | | | | | |
| S&P 500 (TR) | 16,667 | 0.16 | 6.28 | 22.20 | 26.72 | 11.85 | 16.27 | 15.46 | 10.80 |
| S&P 500 (PR) | 7,626 | 0.02 | 5.92 | 21.06 | 24.90 | 10.13 | 14.40 | 13.36 | 8.65 |
| Dow Jones Industrial (PR) | 56,118 | -0.49 | 6.33 | 12.74 | 19.31 | 7.92 | 9.83 | 11.69 | 7.43 |
| NASDAQ Composite (PR) | 23,917 | -1.58 | 4.75 | 20.64 | 25.80 | 7.47 | 17.69 | 17.00 | 12.14 |
| Russell 2000 (TR) | 16,117 | -3.68 | 6.40 | 12.86 | 18.09 | 2.87 | 10.01 | 10.41 | 8.84 |
| MSCI Indices (\$US) Total Return | | | | | | | | | |
| World | 17,045 | 2.68 | 6.67 | 17.09 | 25.00 | 7.42 | 13.66 | 10.15 | 9.17 |
| EAFE (Europe, Australasia, Far East) | 12,020 | 3.26 | 4.61 | 12.42 | 19.99 | 4.68 | 9.14 | 5.71 | 6.60 |
| EM (Emerging Markets) | 2,901 | 1.65 | 6.11 | 9.86 | 15.52 | -2.66 | 5.18 | 2.94 | 7.62 |
| MSCI Indices (\$CA) Total Return | | | | | | | | | |
| World | 23,015 | 0.40 | 5.57 | 19.70 | 24.60 | 9.85 | 14.00 | 12.57 | 9.32 |
| EAFE (Europe, Australasia, Far East) | 16,230 | 0.97 | 3.53 | 14.93 | 19.60 | 7.04 | 9.47 | 8.03 | 6.74 |
| EM (Emerging Markets) | 3,917 | -0.60 | 5.01 | 12.31 | 15.14 | -0.46 | 5.50 | 5.21 | 7.77 |
| Currency | | | | | | | | | |
| Canadian Dollar (\$US/\$CA) | 1.35 | -2.29 | -1.00 | 1.88 | -0.12 | 2.26 | 0.27 | 2.18 | 0.14 |
| Regional Indices (Native Currency, PR) | | | | | | | | | |
| London FTSE 100 (UK) | 8,377 | 0.10 | 1.22 | 8.32 | 12.60 | 5.57 | 3.05 | 2.08 | 3.20 |
| Hang Seng (Hong Kong) | 17,989 | 3.72 | -0.50 | 5.52 | -2.14 | -11.42 | -6.90 | -3.14 | 1.70 |
| Nikkei 225 (Japan) | 38,648 | -1.16 | 0.42 | 15.49 | 18.48 | 11.22 | 13.30 | 9.62 | 6.45 |
| Benchmark Bond Yields | | | 3 Months | 5 Yrs | 10 Yrs | 30 Yrs | | | |
| Government of Canada Yields | | | 4.18 | 3.04 | 3.16 | 3.27 | | | |
| US Treasury Yields | | | 5.12 | 3.70 | 3.91 | 4.20 | | | |
| Bond Indices (\$CA Hedged) Total Return | Index | 1 Mo (%) | 3 Mo (%) | YTD (%) | 1 Yr (%) | 3 Yrs (%) | 5 Yrs (%) | 10 Yrs (%) | |
| FTSE TMX Canada 91-day Treasury Bill Index | 465 | 0.40 | 1.25 | 3.44 | 5.20 | 3.35 | 2.30 | 1.60 | |
| FTSE TMX Canada Universe Bond Index | 1,148 | 0.33 | 3.86 | 2.32 | 7.88 | -1.19 | 0.04 | 2.00 | |
| FTSE TMX Canada All Government Bond Index | 1,078 | 0.35 | 3.99 | 1.86 | 7.29 | -1.76 | -0.50 | 1.69 | |
| FTSE TMX Canada All Corporate Bond Index | 1,395 | 0.26 | 3.47 | 3.68 | 9.61 | 0.42 | 1.55 | 2.85 | |
| U.S. Corporate High Yield Bond Index | 299 | 1.51 | 4.35 | 5.77 | 11.57 | 1.85 | 3.72 | 4.02 | |
| Global Aggregate Bond Index | 260 | 0.99 | 3.72 | 2.68 | 6.57 | -1.45 | -0.15 | 1.87 | |
| JPM EMBI Global Core Bond Index | 534 | 2.39 | 4.94 | 6.16 | 12.52 | -2.80 | -0.49 | 2.12 | |
| S&P/TSX Preferred Total Return Index | 2,027 | 2.71 | 4.99 | 19.92 | 30.50 | 2.17 | 7.46 | 2.68 | |

Source: TD Securities Inc., Morningstar®, TR: total return, PR: price return, as of August 30, 2024

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