



Market Perspectives The Year Ahead Q1 2024



TD Wealth Asset Allocation Committee (“WAAC”) Positioning Overview

- We believe that the equity market has a balanced return outlook. Earnings growth has been negative year-over-year, but we believe that it is now starting to stabilize/show signs of positive momentum. Despite the recent rally, some of the more cyclical areas of the market remain attractive from a valuation standpoint.
- As the normalization of inflation appears to be slowing alongside waning economic growth, the Bank of Canada continues to debate the need to maintain tight monetary policy and to reinforce its higher-for-longer policy rate path. On the flipside, this may also imply higher for longer income returns within the asset class. We continue to believe that fixed income will outperform equities over the next 12 months and that bonds can still provide diversification benefits, reduce overall portfolio volatility and preserve capital.
- We believe that an allocation to alternative assets can benefit diversified portfolios especially when implemented over the long-term. Alternative assets can provide inflation protection and attractive absolute returns, while acting as long-term portfolio stabilizers via their diversification benefits and less correlated income streams.
- In recent months, the yield on cash and equivalents has risen alongside further rate hikes from the Bank of Canada. As key economic data continues to normalize, the risks of additional monetary policy tightening are now more balanced. We believe that the other asset classes may present better opportunities for long-term returns.



The Year In Review

2023 was a challenging year, with a rollercoaster ride of market sentiment to match. Economic indicators and forecasts were often mixed, markets saw significant volatility, and the year both started and ended under the shadow of a potential economic slowdown. That said, many broad market indices showed positive returns and we still saw plenty of opportunities on the table for active investment management.

Both equities and fixed income assets delivered strong returns in early 2023, only to be hit with trouble in the U.S. banking sector. Markets feared contagion, but despite the anxiety at the time, this contagion did not truly materialize over the long-term. Within equity markets and particularly in the U.S., a large portion of the year's returns can be attributed to the so-called "Magnificent Seven": a collection of large cap Technology stocks that rallied on the back of artificial intelligence ("AI") buzz mid-year. In our view, we also saw opportunities over the year in smaller pockets of the U.S. market with reasonable valuations.

Fixed income yields reached decades long highs over the year and despite more recent volatility, particularly in the longer duration space, we maintained an overweight allocation in the asset class throughout the year.

Central banks, including the Bank of Canada ("BoC") and the U.S. Federal Reserve ("the Fed"), doggedly pursued hawkish policy throughout the year in order to curb sticky inflation. Inflation began to slow by the end of the year, however it remains above the target rate for both the BoC and the Fed. We also saw a pause on rate hikes in the later months of the year, which suggests that central banks are starting to see the softening they were waiting on in both inflation and labour markets (which were notably firm over the year). Markets responded well to these central bank pauses, rallying on the news of the most recent Fed rate pause in December and in anticipation for potential rate cuts in the new year.

Geopolitical struggles dominated news cycles and will likely persist in 2024. Global growth began to slow over the fourth quarter and we expect to see that continue into the first half of 2024. It will remain important to closely monitor economic indicators as we go forward into this environment, and we expect to see some ups and downs along the way; however, compared to the forecasts from the start, or even the middle of 2023, a soft landing, albeit bumpy, for Canada and the U.S. is looking more achievable going into 2024.

Chart 1: Global Equity Index Returns

Name	1M	3M	12M	3Y	5Y	10Y
S&P 500 Index (Large Cap)	1.81%	9.25%	23.31%	11.40%	14.97%	14.50%
S&P/TSX Composite Index	3.91%	8.10%	11.75%	9.59%	11.30%	7.62%
MSCI EAFE Index (Europe, Australasia, Far East)	2.57%	8.06%	16.05%	5.87%	8.02%	7.09%
MSCI Emerging Markets Index (Emerging Markets)	1.22%	5.58%	7.67%	-3.49%	3.43%	5.32%

Source: TD Asset Management Inc. ("TDAM"). As of December 31, 2023.

The Year Ahead 2024

Overall Economic Outlook

Both equity and fixed income markets rallied at the end of 2023, seeing a reason for bullishness in the possibility of central bank rate cuts rather than rate hikes in 2024. We likewise believe that the Fed's decision to hold rates steady in December, alongside a more optimistic Fed forecast, may indicate that we will see a pivot to cuts from central banks in the second half of 2024. We believe the Fed may cut rates first, perhaps as early as May or June. We believe the BoC may start introducing cuts towards the summer. It would be a challenge to estimate where rate cuts will end for the year, but we believe that central banks will have to cut carefully, being mindful of the potential to stoke asset price reflation in the housing market, while balancing the economy as a whole. There is little appetite from either the BoC or the Fed to move quickly as backtracking these cuts would be a credibility risk and the potential for a hard landing for the economy remains. While inflation is broadly trending downward, it is still sticky and will remain a key data point for central bank decisioning going forward.

The U.S. economy is expected to continue to outperform other global economies in 2024, though perhaps not to the same degree as it did in the second half of 2023. U.S. growth had already begun to slow in the fourth quarter of 2023, and high

interest rates are expected to continue to impact consumption. We anticipate that U.S., and global, growth will continue to slow, seeing a trough in the first half of 2024 with potential improvement in the second half. The end of this year will also see a U.S. presidential election, which could potentially have an impact on tax rates and tariffs, but also the appointment of the chair and vice chair of the Fed in the coming years.

In Canada, we see challenges for 2024 around consumption growth which, while positive overall, is being buoyed by population growth and is more negative on a per capita basis. Canadian housing markets may also face challenges this year, particularly in Ontario and British Columbia. That said, if the BoC starts pivoting and yields drop from their highs, this will have a positive impact on mortgage rates. This, in addition to the increase in population, should help set a floor for home prices, particularly in the single detached market.

Outside of North America, we continue to see weakness in European markets. In China, much of the world is waiting to see what will happen in property markets and whether a strong government response is incoming.

Outlook

Neutral Outlook For Equities

Sub Class	Allocation
Canadian Equities	Neutral
U.S. Equities	Modest Overweight
International Equities	Modest Underweight
Chinese Equities	Neutral
Emerging Markets ex. China	Neutral

We believe that the equity market has a balanced return outlook and remain comfortable with our neutral positioning. Companies that have adapted to the economic climate of the last few years will likely be in a strong position to start 2024. Earnings growth has been negative year-over-year (“YoY”), but we believe that it is now starting to stabilize and even show signs of positive momentum. We may see earnings growth continue to pick up if a soft landing is achieved for 2024, particularly outside of the “Magnificent Seven”. Strong free cash flows within the Energy sector, and relatively inexpensive Financials stocks, may present attractive opportunities within

the Canadian equity market. International stocks have rallied this year but are challenged by weaker corporate returns and slowing macroeconomic conditions, particularly in Europe. The Chinese economy is showing signs of stabilization and the government remains focused on supporting growth, but challenges remain in the property sector. We feel that the reopening is largely reflected in markets at this point and so we have consequently moderated our exposure to China. We see some opportunities within emerging markets, but more moderate global growth act as a headwind.

Optimistic Outlook For Fixed Income

Sub Class	Allocation
Domestic Government Bonds	Modest Overweight
Investment Grade Corporate Credit	Neutral
Global Bonds- Developed Markets	Neutral
Global Bonds- Emerging Markets	Neutral
High Yield Credit	Modest Underweight

The past year has seen volatility in fixed income markets and we expect higher for longer income returns within the asset class. However, we also continue to believe that fixed income will outperform equities overall for the next 12 months and that bonds can still provide diversification benefits, reduce overall portfolio volatility and preserve capital. Over the longer-term, government bonds continue to remain appealing due to their potential to generate

positive nominal returns. Within investment grade corporate credit, spreads have been fairly stable comparatively, and we continue to see opportunities in lower duration corporate bonds given their appealing all-in yields. We expect high yield credit to be challenged, particularly for corporations with elevated debt loads, increasing overall volatility and downside risk.

Stable Outlook For Alternatives

Sub Class	Allocation
Commercial Mortgages	Modest Overweight
Private Debt (Universe)	Modest Overweight
Domestic Real Estate	Maximum Underweight
Global Real Estate	Modest Underweight
Infrastructure	Modest Overweight

We believe that an allocation to alternative assets can benefit diversified portfolios especially when implemented over the long-term. Commercial mortgages continue to provide accretive income while insulating investor returns from the increased volatility in interest rates. Investor appetite within infrastructure remains strong, particularly for energy transition investments and critical infrastructure sectors that generate stable, growing cash flows. Within the private debt space, high credit quality and global diversification provides safety in a potentially recessionary environment. Incremental income and potential capital appreciation from interest rate moderation provide upside.

In real estate, Canada's growing demographic profile continues to be supportive of domestic real estate, particularly multi-unit residential. Office properties continue to experience leasing and valuation headwinds and a flight to quality, while fundamentals remain sound across the other property types. Globally, we believe that high quality assets, with low leverage and portfolios that are globally diversified may be able outperform in the current environment. Multi-unit residential and a tilt to the Asia Pacific can provide global real estate portfolios with enhanced risk-adjusted returns.

Measured Outlook For Commodities

Commodities can help diversify portfolios with returns that have a low correlation to both stocks and bonds. While energy and some material prices have weakened and may remain weak in the near-term, we also see some support in reasonable inventories and disciplined producers. For example, we see a strong outlook for western Canadian oil producers as they have been able to generate free cash flow and have substantively reduced their debt profiles. We expect further tightness in the copper market due to recent disruptions and downgrades to existing supply.

Equities

Current WAAC Members

Chair



David Sykes, CFA
Chief Investment Officer, TDAM

TDAM Asset Allocation



Michael Craig, CFA
Managing Director and Head of
Asset Allocation & Derivatives, TDAM



Anna Castro
Managing Director, TDAM

TDAM Equities



Justin Flowerday, CFA
Head of Fundamental Equities,
TDAM



Jennifer Nowski, CFA
Vice President & Director,
TDAM

TDAM Fixed Income



Michael Augustine, CFA
Managing Director and
Head of Fixed Income, TDAM



Alex Gorewicz
Vice President and Director,
TDAM

TDAM Alternatives



Jeff Tripp, CFA
Managing Director and Head
of Alternative Investments, TDAM



Colin Lynch
Managing Director and Head
of Global Real Estate, TDAM

Epoch



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



William Booth, CFA
Managing Director,
Epoch Investment Partners, Inc.

Non Voting Members



Brad Simpson
Chief Wealth
Strategist,
TD Wealth



Sid Vaidya
U.S. Wealth Chief
Investment Strategist,
TD Wealth



Bryan Lee
Vice President
and Director,
TDAM

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