TD Asset Management

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Alternative Investments Forecast | 2021

The TD Wealth Asset Allocation Committee ("WAAC," "we") is modestly overweight the alternative investments asset class. With low interest rates and the expectation for elevated volatility for equity markets in 2021, investors may seek alternative investments for their stable cash flows, inflation protection and for the consistent returns they can generate over the long-term. We expect alternative assets such as infrastructure, mortgages, and real estate to play a greater role in portfolios due to their diversification benefits and income advantage they can provide over low or negative real rates in fixed income.

		Underweight	Neutral	Overweight
Alternative Assets (Modest Overweight)	**Commercial Real Estate**	–		+
	Commercial Mortgages	–		+
	Infrastructure	–		+

Commercial Real Estate
(Neutral)

- The pandemic has demonstrated the importance of e-commerce and supply chain logistics, as well as the need for industrial assets such as distribution, warehousing and fulfillment centers.
- Having strategic targeted positions across Global Markets (i.e. U.S., Europe and Asia Pacific) and being diversified across all property types with a focus on industrial and essential-based retail assets, will help mitigate portfolio shocks and prolonged distress in markets in 2021.

Commercial Mortgages
(Modest overweight)

- Heading into 2021, overall liquidity remains high as commercial mortgage spreads trend towards the long-term average.
- We expect the competition for resilient property types (i.e. multi-unit residential and industrial) to remain, which has the potential to drive spreads down even further.

Infrastructure
(Modest overweight)

- Infrastructure continued to offer strong, stable returns during the pandemic driven by the essential nature of the services provided by infrastructure assets.
- Currently, infrastructure equity and debt offer some of the largest expected spreads over government yields versus many other asset classes.

Part of WAAC's mandate is to highlight risks and opportunities on the horizon. Below are some of the factors we will be watching in 2021.

↑ Opportunity ↔ Neutral ↓ Risk

What We're Monitoring	Potential Implications
Canadian Real Estate	↔ We are neutral Canadian real estate entering 2021. Over 2020, COVID-19 had a distinct impact on the Canadian real estate market depending on the property type. The hospitality and retail sectors have been challenged the most and the office market has experienced a disruption in leasing activity as work-from-home has become the temporary normal. ↑ However, the pandemic has demonstrated the importance of e-commerce and supply chain logistics, as well as the need for industrial assets such as distribution, warehousing and fulfillment centers. Moreover, multi-family assets are providing capital preservation and income predictability given their countercyclical characteristics and strong fundamentals.
The Pandemic	↔ The pandemic's impact on the global commercial real estate market has had varying results by geographic region. In the U.S., tourism hubs have been negatively impacted, while cities with a tilt towards the government and technology sector have and should be better insulated. ↔ The outlook on Europe's market will continue to be dependent on the evolution of the pandemic and individual country's fiscal response, while the economic recovery in Asia Pacific should be ahead of other regions given strict government measures and effective societal cooperation. ↑ As vaccine approvals roll out country by country, this has the potential to benefit the speed of the economic recovery. We believe that having strategic targeted positions across all regions (i.e. U.S., Europe and Asia Pacific) and being diversified across all property types, with a focus on industrial and essential-based retail assets, will help mitigate portfolio shocks and prolonged distress in markets in 2021.
Liquidity	↑ We maintain a modest overweight to commercial mortgages. Heading into 2021, overall liquidity remains high as commercial mortgage spreads trend towards the long-term average. ↔ The Government of Canada yield curve steepened earlier this year and has since maintained the upward slope while shifting down by a considerable amount, and the term premium for mortgages stabilized at year end. ↑ Our strategy going into 2021 is to continue to monitor portfolio mortgage assets in this challenging environment, while focusing on underwriting high-quality assets with durable metrics which can provide investors with long-term stable risk-adjusted returns.
Infrastructure Growth	↑ There is potential for significant growth in the infrastructure market as global markets recover. In addition, the pandemic has created a situation where governments have increased public deficits and sovereign debt is expected to increase by $30 trillion over the next three years, creating the need for governments to find new sources of income. ↑ One expectation is that there will be an increased privatization of infrastructure assets, creating further opportunities to acquire these assets. We anticipate this will translate into significant capital being invested in private infrastructure assets in the coming years. ↑ Historically, low interest rates are compounding the opportunity to acquire new infrastructure. Currently, infrastructure equity and debt offer some of the largest expected spreads over government yields versus most other asset classes. The enhanced returns, stable contracted income and embedded inflation protection in infrastructure continues to offer attractive investment opportunities.

Forecast