Timely Premiums

August 23, 2021

AUG 2021

TGED
TUED

Manager Commentary

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At TD Asset Management Inc. ("we", "us", "our"), we are active in our option overlay strategies for both **TD Active Global Enhanced Dividend ETF (TGED) and TD Active U.S. Enhanced Dividend ETF (TUED).** However, what does this actually mean? How active is active? For our approach, we are not restricted in setting the terms of the contracts (e.g., strike price, expiration), the timing of when we write these contracts and how much of a stock holding to cover with our call option contracts. This note for August will touch upon how our active decision making can extract premiums by dynamically adjusting the quantity of contracts for a covered call using Sea Limited as an example.

For those not familiar with Sea Limited (ticker "SE"), the company operates fast growing businesses in e-commerce, gaming and financial services in Southeast Asia. The company was set to report their second quarter financial results on Tuesday, August 17th. As faithful readers to *Timely Premiums* will appreciate, earnings events can be excellent opportunities to extract option premiums, due to an increase in implied volatility related to the uncertainty of, and the reaction to financial results. As such, ahead of the earnings event, on Friday, August 13th, we wrote an out-of-the-money call on SE that covered half our shares. The contract delivered a gross annualized yield of 32% (16% net annualized yield) with about a 17% upside for potential price appreciation ($360 strike price).

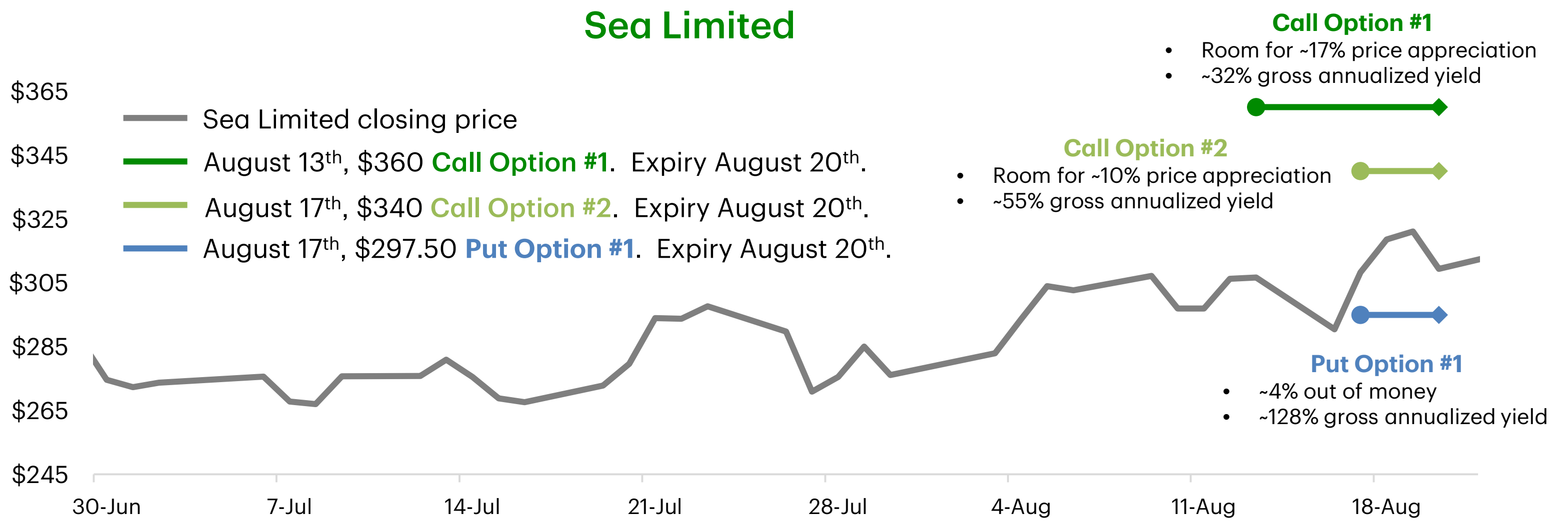
On Tuesday, August 17th, the company delivered exceptional comparable growth that was ahead of expectations and boosted their outlook for the full year. The stock market reacted positively and the share price of SE increased by about 6% on the day. Since SE was trading at similar price levels to the Friday, there was still a 17% difference between the current price and strike price with four days left before the contract expiration. The likelihood of the stock reaching the $360 strike price over the remaining contract period was a very low probability outcome. Given the surprise of management's confidence for their financial performance in the second half of year, the implied volatility for SE remained elevated. One method to extract additional premium would be to close the current call contract and then write a new out-of-the-money call contract. The challenge of covering the option at the time was that this action would have netted a fraction of the income potential compared to letting the contract expire out-of-the-money on Friday, August 20th. In order to maximize the income from the implied volatility on earnings day, we left the current call option untouched and wrote a new call option contract on Tuesday, August 17th with a strike price of $340 and a similar expiration date. This new call contract had a gross annualized yield of 55% with about a 10% price appreciation potential. Since the first contract written was effectively worthless (i.e., the ETFs had captured the full option premium), the contract written for this second call option covered the remaining shares outstanding. From our perspective, while on paper these contracts resulted in 100% call coverage, the second contract effectively maintained the original 50% call coverage. The outcome of our active decision was a 44% net annualized yield for a fast-growing non-dividend paying business.

However, elevated implied volatility levels can also create opportunities for option premium capture on the put side. As such, for the put overlay, we wrote a put contract on Tuesday, August 17th with a strike price of $297.50, that would have us potentially buy the stock 4% lower than the current price with an "eye-popping" annualized yield of 128%. The contributions of the premiums from just these three option contracts (two calls and one put) was the equivalent of 1 basis point of relative performance for the ETFs. That is impressive for extracting income out of the implied volatility from just one of the holdings in our portfolio.

Hopefully, with this month's note, we have provided you with more awareness regarding the level of activeness that we can apply with our option overlay strategies. Moreover, how our active decisions can potentially extract more value compared to a systematic overlay strategy and how competing products that also employ active options strategies may not be equivalent.

Thank you again for your continued interest and support. We look forward to providing you with another update in September.

Chart 1: TGED Option Overlay Strategy Example



Source: TD Asset Management Inc., as of August 23, 2021.

Performance	1 Month	3 Months	6 Months	1 Year	2 Year	Since Inception	Inception Date
TD Active Global Enhanced Dividend ETF	3.4%	6.5%	12.9%	26.3%	18.9%	17.3%	05/03/2019
TD Active U.S. Enhanced Dividend ETF	4.2%	8.3%	17.0%	29.2%	n/a	30.7%	05/26/2020

Source: TD Asset Management Inc., as of July 31, 2021. Returns for periods greater than one year are annualized.

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