TD Asset Management

U.S. Liquidity Management

Commentary

2024 Q2

For the quarter ended June 2024

Fixed Income Outlook

TD Asset Management emphasizes capital preservation in our active fixed income portfolios while seeking to maintain a yield advantage relative to the benchmark. We expect U.S. real Gross Domestic Product (GDP) will slow to below trend in 2024, with little improvement expected in 2025. Elevated inflation, higher interest rates, reduced private-sector consumption, and a decline in business investment may contribute to a recession during 2024. Elevated inflation and a strong U.S. labor market are factors contributing to higher short-term rates, via U.S. Federal Reserve (Fed) funds rate hikes. The bond market will be subject to heightened volatility due to persistently high inflation, tighter financial conditions, and geopolitical events. The period of climbing front-end yields has ended as the Federal Open Market Committee (FOMC) completed its hiking cycle. However, the FOMC is committed to its restrictive policy framework – an elevated federal funds target rate and balance sheet reduction. We remain constructive, and very selective toward credit and are comfortable with our strategic credit positioning. Corporate bonds continue to offer some value over government bonds; thus, we maintain our preference for high-quality investment grade corporates. We continue to be positioned with an emphasis on liquidity and quality.

Focal Points

- Headline U.S. GDP growth slowed to 1.4% in Q1 2024 as more volatile trade and inventory components shaved 1.1ppts off the number. Most other internals increased quarter-over-quarter (QoQ). Additionally, inflation was adjusted modestly higher bringing nominal GDP to 4.5% from 4.3%.

- The current federal funds target range is 5.25%-5.50%. The Fed's median federal funds forecast for year end 2024 is 5.125%. The FOMC will keep its policy rate restrictive until it believes inflation is on a sustained downward path to two-percent which will take time.

- U.S. Treasury yields increased during the quarter. Recently released data indicate a slight softening of inflation (but still too high), a resilient labor market, and slowing household consumption.

- Corporate bond spreads increased during the quarter as primary market issuance is running well ahead of last year's pace. Investors are positioned for low economic growth and are assigning a lower risk premium to geopolitical factors, tighter bank lending standards and the FOMC's restrictive monetary policy.

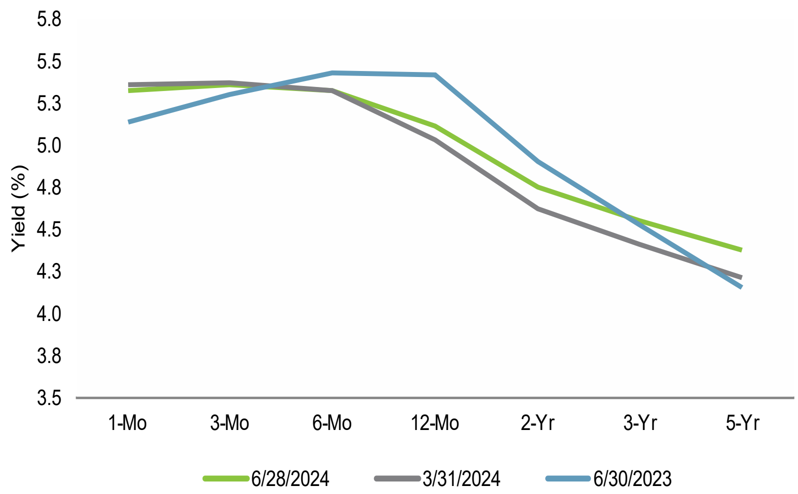
Investment Professionals:

Glenn Davis, CFA
Managing Director

Dennis Woessner, CFA, CAIA
Vice President & Director

Source: TD Asset Management, TD Economics & Bloomberg Financial L.P.; June 30, 2024

Front-end Treasury Yields



Source: Bloomberg Financial L.P.; June 30, 2024

U.S. Treasury yields increased during the quarter. Recent economic data indicate a slight softening of inflation (but still too high), a loosening labor market, and slowing household consumption. The data has had minimal impact on the outlook for interest rate cuts, so far.

We expect front-end yields to move lower from current levels as inflation eases and the FOMC begins to cut interest rates to maintain its current restrictive policy framework.

Macro Update

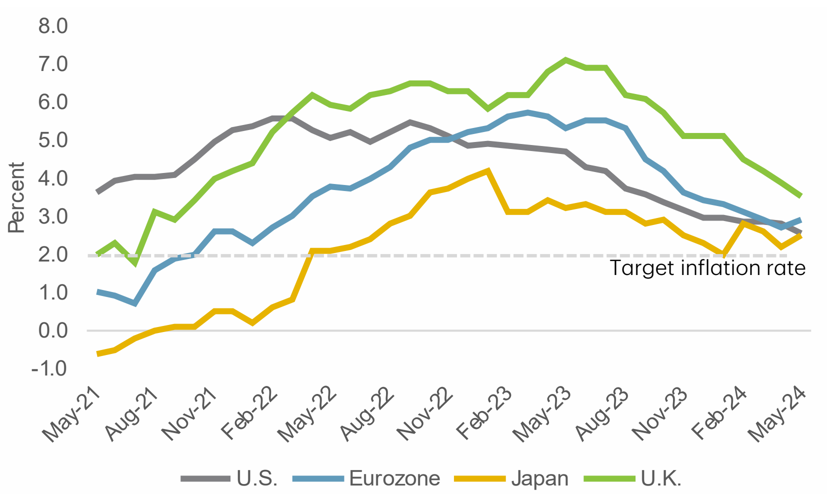
- U.S. real GDP increased 1.4% in Q1 2024 (3.4% in Q4 2023). The larger-than-expected decrease was primarily due to the more volatile inventories and trade segments which shaved 1.1 ppts off the number. Consumer spending and residential investment were positive. Domestic demand remains relatively strong and quarterly measures of inflation are above the FOMC's target rate.
- We expect U.S. growth will weaken during 2024, with little improvement in 2025. A U.S. recession within the year is possible as the FOMC maintains its restrictive policy framework, consumer demand wanes and business investment declines as corporate profits fall; however, the labor market remains strong.

Source: TD Economics & Bloomberg Financial L.P.; June 30, 2024

Our Long-Term Views:

- U.S. and global economic growth remain relatively weak and recessionary risks remain in certain areas. A broad economic slowdown driven by higher short term interest rates, elevated inflation, and a broader contraction in credit could lead to muted relative returns.
- The Fed policy will be restrictive to mitigate inflation. Tighter financial conditions my result, as nominal and real interest rates remain elevated.
- Inflation in developed markets continues to decline due to a more balanced supply and demand profile. Higher wages, higher food prices, and geopolitical events are still factors of concern.

Inflation



Source: Bloomberg Financial L.P.; June 30, 2024

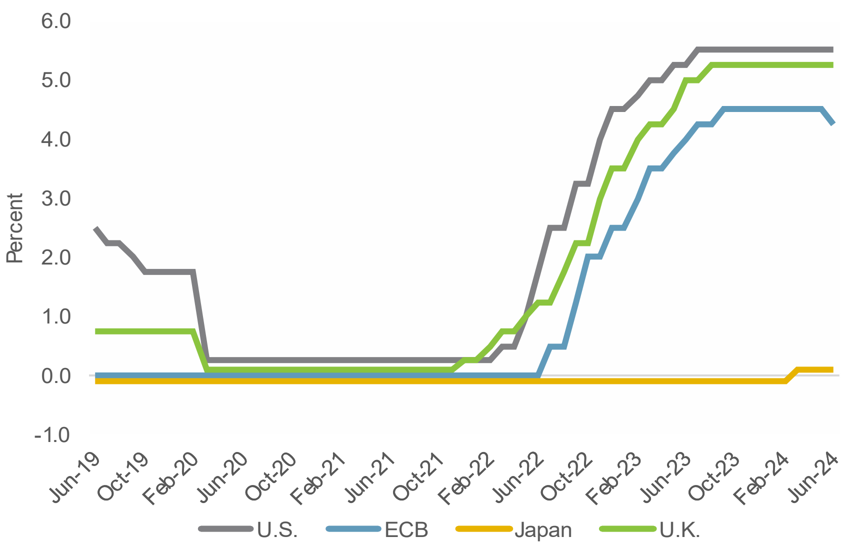
Headline inflation in the U.S. and other major economies has peaked and is decreasing. U.S. core prices remain elevated but are trending lower as well. We expect inflation to decline over the next twelve months; however, achieving the FOMC's two-percent target may take longer than the market and FOMC expect.

U.S. Central Bank Update

- The federal funds target range remains at 5.25%-5.50% which is probably the peak range based on Chair Powell's comments. The FOMC's statement dropped its tightening bias so the next rate move is lower, most likely. The downward trend in inflation readings slowed during Q1 2024. This will delay the FOMC's first interest rate cut until the second half of 2024.
- The Fed's summary of economic projections for 2024 show above-trend growth, a flatter path of disinflation, a slightly weaker labor market, and a marginally declining federal funds rate, to 5.125% by year end which means one rate cut from the current rate.

Source: TD Economics & Bloomberg Financial L.P.; June 30, 2024

Central Bank Policy Rates



Source: Bloomberg Financial L.P.; June 30, 2024

Central Banks have kept inflation expectations well anchored by raising their respective policy rates (becoming more restrictive) thereby slowing growth by reducing demand as inflation remains above target.

Most major Central Banks have ended their respective tightening cycles and are data dependent when determining future policy decisions.

The European Central Bank (ECB) and the Bank of Canada (BoC) cut their respective policy rates in June as we expected. The Bank of Japan (BoJ) may hike its policy rate later this year.

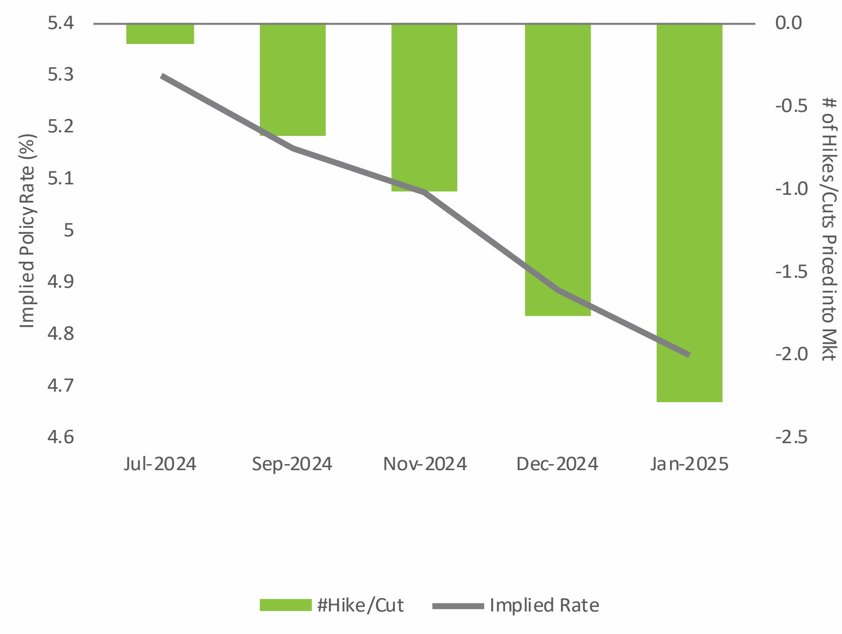
Cash/Short-term Market Update

- Short-term Treasury yields were mostly higher for the quarter. The median FOMC forecast shows one rate cut in 2024. Based on recent inflation data, the disinflation path seems be resuming after a brief spike earlier in the year.
- Short-term credit spreads widened 3 basis points (bps) during the quarter as many investors position for low economic growth, with no recession, and assign a lower risk premium to geopolitical factors and tighter bank lending standards.
- Prime money fund assets increased $19.3 billion during the 3-month period ending June 2024. Total assets are $1,043 billion (up 27% year-over-year (YoY)).

Source: Bloomberg Financial L.P.; June 30, 2024

- **Current Positioning:**
  - Short and Short/Intermediate Government/ Credit models prefer high-quality investment grade corporate bonds and have a longer duration relative to their respective benchmark.

Number of Hikes/Cuts Priced into Market



Source: Bloomberg Financial L.P.; June 30, 2024

No additional federal funds rate hikes are expected during this tightening cycle. The implied future policy rate indicates a potential rate cut by September 2024 which matches our expectation.

The implied peak policy rate of 5.3% is now expected to slowly decline throughout 2024 and into 2025 as real economic growth slows and inflation moderates further.

1-3 Year Corporate Option-Adjusted Spread (OAS)

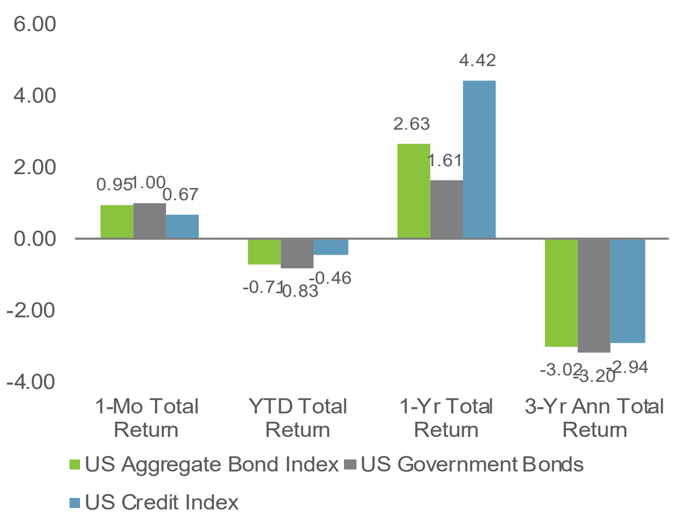
Source: Bloomberg Financial L.P.; June 30, 2024

During the quarter, the index OAS widened 3 bps, to 60 bps. YoY, the index OAS is 12 bps tighter. Factors such as above-target inflation, a sluggish GDP outlook, a restrictive FOMC policy, and current geopolitical events continue to minimally impact spreads.

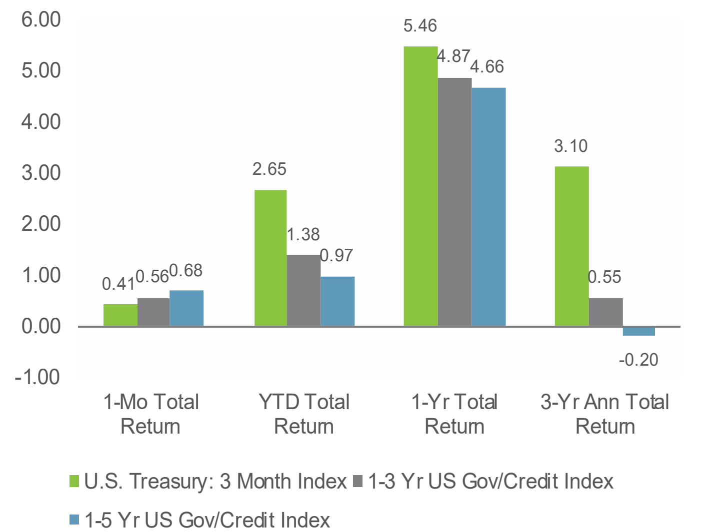
Corporate fundamentals are expected to weaken as we enter an economic slowdown. Financial conditions are accommodative even as the FOMC maintains its higher for longer pledge with respect to interest rates.

Charts & Tables

Fixed Income Bond Indices



Total Return (%)



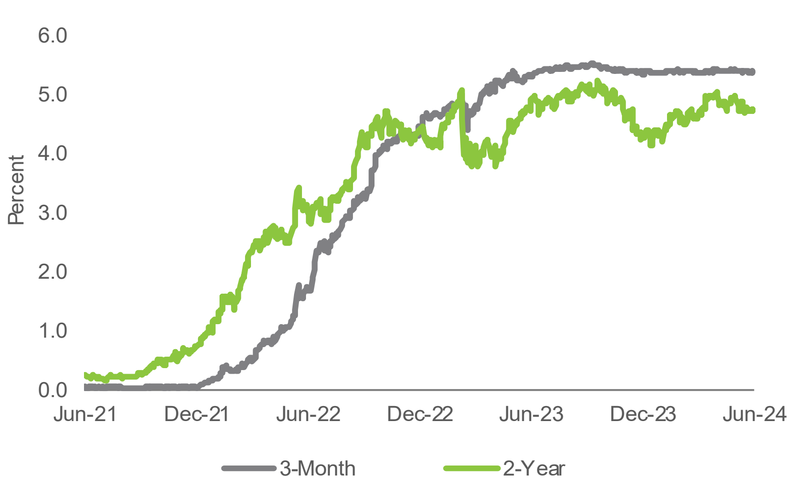
Economic Figures & Short-term Rates

Description	Current	3-mo Ago	1-yr Ago	Next Release
Fed Funds (%)	5.50	5.50	5.25	7/31/2024
CPI (YoY %)	3.30	3.20	4.00	7/11/2024
PCE (YoY %)	2.60	2.50	4.00	7/26/2024
Unemployment Rate (%)	4.00	3.90	3.70	7/5/2024
GDP (YoY %)	2.90	3.10	1.70	7/25/2024
Retail Sales (YoY %)	2.30	2.10	2.40	7/16/2024
Leading Indicators (YoY %)	-5.30	-6.50	-8.20	7/18/2024
Housing Starts (000s)	1,277	1,546	1,583	7/17/2024

Description	Current	3-mo Ago	1-yr Ago
Fed Funds (%)	5.50	5.50	5.25
3-Mo U.S. Treasury Bill	5.36	5.37	5.30
6-Mo U.S. Treasury Bill	5.33	5.32	5.43
USD O/N Govt. Repo	5.34	5.39	5.17
U.S. 30-Day Comm Paper*	5.32	5.35	5.10
U.S. 90-Day Comm Paper*	5.38	5.41	5.36

*A1/P1/F1 rated U.S. Commercial Paper

Treasury Market



Change in Yield Curve (basis points)				
Maturity	Yield Curve (%)	1-Mo Ago	3-Mo Ago	1-Yr Ago
1-Mo	5.32	-4	-3	18
3-Mo	5.36	-5	-1	6
6-Mo	5.33	-6	0	-11
12-Mo	5.12	-6	9	-30
2-Yr	4.76	-12	13	-15
3-Yr	4.55	-13	14	2
5-Yr	4.38	-13	16	22
7-Yr	4.37	-13	16	38
10-Yr	4.40	-10	20	56
20-Yr	4.66	-6	21	59
30-Yr	4.56	-9	22	70

Source for all charts and tables: Bloomberg Financial L.P.; June 30, 2024

Liquidity

TD Asset Management:

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