TD BANK GROUP
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FIRESIDE CHAT

Rob Sedran – CIBC World Markets - Analyst

I'm very excited to welcome Bharat Masrani from TD Bank to the conference today. He is the Group Head of U.S. Personal and Commercial Banking, and a member of the Bank's Board of Directors. During his 23 years at the Bank, Bharat has held various roles, including Vice Chair and Chief Risk Officer. In his current role, he is responsible, of course, for TD's strong push into the US and arguably its single largest growth driver over the next few years.

Before we begin, I have been asked to remind you that Bharat may make forward-looking statements that represent management's views as of today, and these statements are meant to assist listeners in understanding the Company's financial position, objectives and priorities and anticipated financial performance and may not be appropriate for other purposes. Actual results could differ materially from what is discussed and listeners should consult the Company's regulatory filings for the risk factors underlying these statements, which are filed with securities exchanges and on their websites.

Bharat, welcome to Montreal. I'll give it to you for some opening remarks. And then we'll launch into Q&A.

Bharat Masrani – TD Bank Group - Group Head, U.S. P&C Banking

Thank you, Rob. And I'm glad he had to do this and not me, on the forward-looking statements.

Rob Sedran – CIBC World Markets - Analyst

I tried to memorize it, but I couldn't do it.

Bharat Masrani – TD Bank Group - Group Head, U.S. P&C Banking

You have done a great job. Really, really appreciate the opportunity to be here in Montreal, one of my favorite cities in the world, and home to some of our largest investors. I really appreciate the opportunity and great to see some familiar faces in the audience.

What I will try and do is give you an update on the TD story, how we are doing in the US, and then open it up for questions. I know Rob has a few, and if you have any, I would be happy to take those as well.

But before I talk about the US, you saw the numbers. We released them a few weeks ago. TD Bank Group had record adjusted earnings of CAD1.8 billion that was up 11% year-over-year. And within that number, retail earnings also were at a record level of CAD1.6 billion. And we did announce an increase in our dividends, CAD0.05 a share, and increased the target payout range to between 40% and 50%. And it just outlines the confidence our Board has in our strategy.

Let me switch to TD Bank, America's Most Convenient Bank. And there are some new faces here, so for those of you not totally familiar with our business in the U.S., we have over CAD208 billion in assets now, in our P&C business in the U.S., CAD169 billion in deposits and more than CAD86 billion in loans. We also have 1300 stores from Maine to Florida and have more than 8 million customers in the U.S. for our personal and commercial banking business.

And our customer proposition has not changed. We are America's Most Convenient Bank, and we wow our customers not just with great, but with legendary customer experiences. With respect to our numbers, in our third quarter, our U.S. business generated CAD355 million in profits; that was up 3% year over year. We

continue to post strong organic growth in loans, 14% year-over-year growth, and core deposits were up by 9% from the previous year.

As you would expect, given the low interest rate environment, we are experiencing some pressure on our margins. But having said that, part of our core strategy is to invest in our franchise, and we are continuing to do that. We opened 12 new stores in our footprint in the quarter and are on track to open more than 35 in this fiscal year. And my expectation is that that number will continue to be around the 35 level for next year as well.

As we look out, our view is that we will continue to take share. One of our great headlines out of our U.S. business is that we continue to take share in the markets in which we operate. But there are headwinds, and I know people will ask me questions on this. The low interest rate environment is not friendly for a bank that is arguably one of the most liquid banks in the world with a huge amount of deposits, so there's a lot of pressure on that.

The regulatory challenges continue. We still have a lot of rules around Dodd-Frank that have either not yet been proposed or implemented, so there are challenges that continue. I know all of you have heard of the fiscal cliff, so we will see how that plays out and how the political environment settles down after the elections. And Europe - what can I say about Europe? You know as much as I do, but that does create a lot of uncertainty for all types of businesses, including our own.

Before I take your questions, and I know, Rob, if one of your audience doesn't ask me that, I know you will. It's regarding the target we set a few years ago for our U.S. business at CAD1.6 billion. I'd start off by saying I'm committed to that target, that we're working very hard to make sure that we do achieve the target we laid out. But I think some context is probably appropriate.

When we talked about that, I think it was in 2010, sounds like many, many years ago - it was about a couple of years ago - certain things have certainly changed. A lot of negative headwinds out there. I think the Durbin amendment and Reg E were kind of theoretical concepts there, and they have become reality. That in itself, and I've made this public before, just those two regulatory changes have resulted in pre-tax profit pressure of $400 million.

If you look at what's going on with margins in the U.S., we've had essentially zero rates for 3.5 - 4 years. And as I have said before, that puts a lot of pressure on some of our business, especially the deposit taking business. And that's probably, hard to quantify, but several hundred million dollars. So the headwinds have been immense.

On the flip side, we didn't have TD auto finance when we announced that, so that should provide us with some good growth as well. And frankly, I'm very pleased with our team. They have delivered core growth in loans and deposits, and new customers. We have been able to reposition some of our products. We have optimized our pricing, in many cases. And you are seeing some of those benefits. So overall, I'm committed to the target. I just want to lay this out front, and we are working very hard to make sure that we get there.

So with that, happy to take your questions, Rob, or any questions from the audience.

Rob Sedran – CIBC World Markets - Analyst

Okay. Thanks, Bharat. And I would encourage anyone that has a question to please just throw your hands up. And like I said before, I'm happy to defer to the questions from the audience.

I want to start, because nobody has put their hand up yet, with the mortgage business. The growth rates you have been putting up in that line of business, admittedly from a low base, have been remarkably high. I wasn't going to ask this until last week, but when you see QE, and part of QE is aimed directly at the mortgage market, do you see this as having any impact? It didn't feel to me like the mortgage market was suffering from a lack of liquidity. Does this have any impact on you and your ability to originate?

Bharat Masrani – TD Bank Group - Group Head, U.S. P&C Banking

So just to give you some background, when we entered the U.S., the legacy institutions we bought were, for the most part, not that active in the mortgage business. They were smallish banks, community banks, and they were just not very active. But as you would expect, with TD, we have a great experience in the mortgage markets. We know what works, and frankly decided to build a platform from Maine to Florida and wanted to leverage the positioning we have, which is unparalleled convenience and legendary customer experiences.

So what that did for us is, as the rates dropped -- and many of you know the way the U.S. mortgage market is structured, you have a tremendous amount of refinancing activity that goes on. So we have millions of customers who are TD customers, they love our bank, they do want to be wowed for everything that they have from any institution. So when they decided to refi their mortgage, which happened to be elsewhere because we were not in the business, they decided to refi with us. And hence, you are seeing a huge amount of activity because our own mortgages are not getting re-fied because we did not have much. But other banks' mortgages that are being re-fied are coming to us, and hence you are seeing this growth.

And so with QE3, it was interesting. 30-year rates actually went up, which was paradoxical, actually, in some manner. But there is the fundamental issue in the US where the dislocation hasn't worked itself out. So you still do not have all the players that you would traditionally see in the mortgage market. They have not reentered yet. So in a way, you are having a business that is seeing very good spreads from an historic perspective. And what we also see in our business is, when we have a mortgage with a customer, they have seven-plus products and services with our bank. And when they don't have a mortgage with us, it's about four products and services they have with the bank. So it is also turning out to be a relationship product.

Specifically, your question on QE3 - if the intent is for rates to be even lower, you would think that the refi activity would continue and the growth that we are seeing for our banks should continue because refi is very beneficial to us. If you feel at some point that rates will go up, because some market participants tend to think because of inflationary expectations rates might go up a bit - and if they do, then you would think that some other parts of the mortgage market may come back, like prices are firming up. I think a lot of inventory has moved out now, a lot of the excess housing stuff that went on in various markets is more stable now. So once that happens, you would think the purchases will go up and we should benefit from that as well. So it's a long way of saying I don't see huge impact for our bank in continuing to do well on the mortgage front.

Rob Sedran – CIBC World Markets - Analyst

This product has not traditionally been considered a balance sheet product. Should investors worry about some of the risks around the growth, either from an interest-rate perspective, a credit risk perspective or even just operational, when you are growing that rapidly?

Bharat Masrani – TD Bank Group - Group Head, U.S. P&C Banking

So just quickly, on credit risk, these are close to super-prime mortgages. I think the other phenomenon, this is not only for TD, but for the industry, is that the rules around mortgages have changed quite dramatically. So essentially, banks, specifically TD, we will not do a mortgage that had any or a reasonable chance of going delinquent even for 30 days because in the U.S., if the mortgage goes into that category, the compliance around that is quite high. The cost of servicing such a mortgage is dramatically higher than a prime mortgage. So it just forces institutions just to do undoubted type of mortgages because you just don't want to go into that category. So I don't worry about credit as much from a mortgage perspective.

Interest rate risk, yes; the U.S. is unique, unlike Canada, there is no prepayment penalties. You get a 30-year fixed rate mortgage. Generally, people worry that banks don't have funding of that type, so how could you manage the risk?

A couple of points I'd make, not only for our U.S. balance sheet, but if you were to take all of TD Bank Group's balance sheet, this is still a very small part of our balance sheet. Secondly, we do hedge the risks. You know, Rob, we are quite conservative. Our risk appetite is pretty tight on what kind of interest rate risk we would take, so there is an active hedging program against that book.

And lastly, at this level of rates, there are certain risks that are actually welcome from that product, given our overall risk that we manage in our balance sheet because there is offsetting positions that come through other products on our balance sheet.

So overall, I feel comfortable. I think the operational risk you talk about is a real issue and to an extent, is the same answer when I started off, that you have to make sure from a servicing perspective that you are dealing with more prime-related type of mortgages. You are not into the near-prime or other space because the cost of compliance, the operational issues around that are quite uncertain. In fact, there are new rules coming out by the end of the year on mortgage servicing for such mortgages. So there will be more certainty by then. But from my perspective, the space we are playing in, I think the operational issues are quite manageable.

Rob Sedran – CIBC World Markets - Analyst

Okay, let's talk deposits. The loan growth rate has been outpacing the deposit growth rate. But just based on the size of the two books, I think in dollar value deposits are still growing more rapidly than loans. When you think about that in balance, how do you change your pricing behavior on deposits? I know you probably don't want to slow the growth in deposits. But if you are not able to deploy them as rapidly, should you slow your growth in deposits a little bit?

Bharat Masrani – TD Bank Group - Group Head, U.S. P&C Banking

It is interesting how some things are in fashion and other things are not. For the longest time, deposits were great to have and nothing wrong with them. And I think the part that gets missed is when you are a growth company, especially in our space, one of the great proxies of that growth is deposits, because you are getting new customers who come in. And when they open accounts, they're going to place deposits with you. That's a good proxy.

And by the way, when your deposits are going up, there is a good chance your fee income is going up because those accounts are generating fees. So nothing wrong in attracting deposits. I think your fundamental point on how do you manage your balance sheet, and I think we've shown consistently that and having been in the risk business a few years ago that we can on a control risk basis, on a risk-adjusted basis, grow our loans and grow our assets at a smart rate.

And we have been doing that. And I think the opportunity in that regard is great for us. We have a great rating. One of the few banks, the only bank that's still AAA rated, and that resonates with our customers in the U.S. We were one of the few banks that continued to lend during the crisis. So that helped us grow that.

And so I think I'm very happy with how quickly we are growing. Particularly on the deposit side, the central part of your question, we have employed a lot of strategies. We are repricing our deposits. If you look at my cost of deposits relative to the industry, it's one of the lowest cost of deposits that we have. And we are really focused on core deposits, which is not flighty; these are all sticky deposits.

So yes, would I like? It's not slowing deposits down, but can I do more on the loan side? Yes, of course. And I think TD auto finance is a good vehicle for us to generate more assets. And there are good opportunities in the U.S. market.

Rob Sedran – CIBC World Markets - Analyst

The asset acquisition, or the asset generator acquisition, like the TD auto finance, the old Chrysler Financial business, the Bank has spoken in the past about being interested in those kinds of acquisitions. But it feels, at least it looks to me or it can look, like a one-off kind of deal. It's a great deal, but there's not a ton of these things around there to do. Am I wrong? Are there other asset originators that would fit well with like a national asset origination model for the deposit base?

Bharat Masrani – TD Bank Group - Group Head, U.S. P&C Banking

You are right. TD auto finance is a great business to be in. And it fits not only our risk appetite, but the experience through the downturn as to how that asset class behaved also, is very attractive. And, frankly, it's one of the few asset classes that you could go out of your footprint and have a national business that you can manage from a risk perspective. So it fits a lot of categories that you could mark off. And we have great hopes in that business, and I think you will be pleased as to how we are making good progress into that business.

Now, the good thing for us is that, yes, there is another one that fits that kind of profile? Would we be interested? And we've said yes, we would be. But if we don't get one, that doesn't mean we are strategically challenged because we now do have our own capabilities to generate assets and loans, as we have shown. 14% is nothing to sneeze at. That's a good number to post and to be able to consistently take share.

So yes, it would be nice if we can find similar profile asset generators. But if we don't, then organic growth is our core strategy. We have been delivering against that, and I feel good that we will continue to make good progress in having that deposit-loan ratio more in balance.

Rob Sedran – CIBC World Markets - Analyst

You touched on the margin issue that the industry is suffering from earlier in your prepared comments. And when I think about your margin specifically, though, you have the benefit of redeploying some of those deposits into loans and growing the loan balance more rapidly than many of your competitors are growing. So should your performance be better than the industry on the margin front?

And I note this quarter it was an issue that bothered, some people saw the margin come down. I think there were some accounting issues playing with the quarter-on-quarter look and all the rest. But structurally, the margin, forgetting all the accounting issues around the acquisitions, should we see you outperforming on the margin because of the way your balance sheet is evolving?

Bharat Masrani – TD Bank Group - Group Head, U.S. P&C Banking

It's bumpy, and as I mentioned on the call, you were right; there were some questions on how should we look at the margin. It is an important measure, but it's quite bumpy and quite noisy. Acquired loan accounting creates volatility on that. And generally I've said that a good range for us is 3.50% to 3.75%; that's the way to look at our margin. And I said this, I think, two or three years ago. And we essentially remained within that range. Yes. Could you breach that one or two quarters? But generally, that's a good way to look at it.

And your big question, should we be outperforming or underperforming? I think what I've learned in the U.S. market is that banks do run different strategies, and some of them
change their strategies more often than perhaps we might. So you could always have outliers out there and say, well, I thought you were going to outperform. And how come you didn't?

But generally, I'm comfortable with the way we are running our business. But the important point is there is pressure on margin. When you run the type of business we do, we're a deposit-heavy bank. And on the deposits side, at some point you take your cost of deposits down to zero. You don't go negative. So there is

only limited amount of opportunity to re-price your deposits because there is a bottom line after which you cannot re-price.

So I see continued pressure over the near-term on deposit margins just because of the rate environment. As we reset our tractors and how we redeploy those funds, it just gets to reset it at a lower rate. So I see continued pressure from that perspective. But the range I put out is not an unreasonable way of looking at where you should expect our numbers to come in.

Unidentified Participant

Can you talk a bit about the evolution of Fannie Mae and Freddie Mac down there, and how that might affect your mortgage business?

Bharat Masrani – TD Bank Group - Group Head, U.S. P&C Banking

So they are now the market, Fannie and Freddie. The last time I heard, it was about $5.5 trillion of mortgage exposures between the two of them. So they are the market. As you know, there is a lot of discussion on reorganizing them, and they are now, for the most part, explicitly guaranteed by the U.S. government. And some proposals are out there, and the view is that after the election perhaps there might be more momentum in how they get reorganized.

I don't see either Fannie, Freddie or a derivative of that or some new organization coming. I don't see a complete disappearance of that type of structure in the U.S. Rob asked, okay, how do you manage the interest rate risk and the like? If my book was many times bigger than what it is today, then it would be quite normal for us to be selling the mortgages away to Fannie and Freddie because, at some point, you say I don't want that risk anymore because it's a negative convexity. Because the way the U.S. mortgages work is rates never are in your favor. So when rates drop, people prepay and refinance. And when rates go up, they hang on.

So for a bank, you've got to manage that risk so that you don't get caught on the other side of that trade. And so, if you have that basic structure in your mortgage market, then you need a Fannie and Freddie, where people will sell it because they just can't hold onto that risk for themselves.

And so I see some version of Fannie and Freddie continuing. Right now, it's not healthy because there is so much uncertainty on the industry of put-back risk, compliance risk, whereas in normal times that risk is quite benign. But now, it's a politically charged environment, and you think you have sold off the mortgage to Fannie and Freddie, but it can easily come back because there's the put-back risk.

So I see a version of Fannie and Freddie surviving. Unless the whole market gets reorganized, then all of a sudden you have a Canadian style mortgage there where you can fix the rate for five or seven years. And if you want to prepay, you pay a fee, a breakage fee to the bank. And then that risk is totally manageable for an institution.
Investor Conference
So I don't see them disappearing anytime soon. And that will have an influence in the mortgage market. I see, currently, you have a lot of the traditional players who were in the mortgage market are no longer participating. Once this is more certain, and this is the structure, I see them coming back, which will put pressure on margins as well. The spreads in the mortgage business - that's how I see it playing out.

But these things do take time. By the time, the election is over and the new Congress sits in and there will be a lot of discussions on how to reorganize this, and it will take some time before there's certainty around what happens to Fannie and Freddie.

Rob Sedran – CIBC World Markets - Analyst

I want to touch on the issue of acquisitions. I know it's no longer, at least, the central part of the TD strategy. After a flurry of activity a while back, it has been reasonably quiet on that front. And I think part of the challenge, I guess, in the market generally is that the bid/ask spread is still or had been fairly wide. And it feels that there was a transaction in your footprint very recently, actually, where the acquirer managed to have it accretive to capital and earnings. So does it feel like expectations from the sellers are rationalizing somewhat to the environment and they no longer want peak pricing, and perhaps we are getting closer to a more active market from an M&A perspective?

Bharat Masrani – TD Bank Group - Group Head, U.S. P&C Banking

Firstly, from our perspective, yes, we did the deals, because our view was that in our business you need sufficient scale before you can have organic growth because if you don't have sufficient scale, you will just not have enough momentum in the markets that you operate in. And hence, it was necessary for us to set up that base.

Good thing now is, as I started off, I said I have 1300 stores Maine to Florida, over CAD200 billion in assets, 8 million customers. So we do have scale. So we are not strategically challenged from that perspective that we have to go out and do a deal; otherwise, we're going to be left behind. We're now, in our own right, within the U.S. market, a top 10 bank in the country.

So we are large. We do have scale. And hence, we are going to be more selective in what we do. So we've said consistently that any transformational deal is off the table, given all the macro head winds that we see. Would we look at small tuck-ins, in certain types of markets like Florida? Absolutely. We did the FDIC deals, we bought South Financial; it was a relatively small deal a couple of years ago. And that has worked out very well for us.

From a market perspective, from a macro market perspective, yes, once in a while, we saw the deal you talked about. We saw it in the press. I can see, once in a while, some deals getting done. But I haven't seen a flurry of deals out there because the bid/ask is still not well aligned. And there's a lot of uncertainty, and not sure that some of these institutions that are being sold are the type of business models that are attractive for us. Notwithstanding the fact that they are small and fit into the small tuck-in category, but the business model or the franchise value don't appear to be attractive for us.

Rob Sedran – CIBC World Markets - Analyst

Got about a minute left, I want to talk about expenses, quickly. And the question I want to ask is, do you feel like your business is more or less, or is positioned where the parent bank or the TD Canada Trust was positioned a number of years back, where you are generating very strong revenue growth but you're also having to invest to generate that growth, and so the operating leverage, we shouldn't consider a huge opportunity for operating leverage, you are reinvesting and are going to continue to do so?

Bharat Masrani – TD Bank Group - Group Head, U.S. P&C Banking

That's not a bad way to summarize that, Rob. Having said that, we are looking at initiatives, as is every business within the TD family of how do we permanently reduce our costs, and how do we do that in a manner that's consistent with our strategy and consistent with our proposition?

And so the U.S. is part of that program. We are part of TD Bank Group. And so we continue to do that, but we are not going to stop investing in our franchise. We will not stop investing in new stores. We've made huge investments in our technology platforms to create not only the wow customer experience, but, as well, creating efficiencies. We recently rolled out our customer capture, as we call it, C-squared, in all of our stores

where, if you were to walk in and see one of our tellers, previously if you had more than five or six checks you were depositing, tellers would put a rubber band around it and throw it in the little bag at the back. And then lo and behold, you thought you had five checks, our back-office looks at it, there's only four. And we get into a discussion a few days later, and hopefully you find that check. And as you can imagine, the cost and the lousy experience that attracts. But most banks, that's how they do it.

So we introduced at each of our teller wickets, what we call the image capture capability. It's not just scanning, but this is an intelligent way of capturing. So now your six checks, before you leave, they are all scanned, all automatically. So if there is one missing you are going to know before you leave the bank. And every 20 minutes, one hour, automatically gets transferred. The image gets transferred to our data center and it gets processed there. Then it comes here into Toronto, where our overnight processing takes place. And lo and behold, you have fantastic customer experience because there are no errors. We have very good back-office synergies because we are not into three or four days of reconciling your account.

And, we just reduced the risk to the bank because it's easier to balance the bank, which is kind of a key requirement for a bank like ours. So this is a win-win-win. So that's just an example of what we have to do, and we will continue to do that. But that doesn't mean you won't see very good expense management from our U.S. business because we are of a size and scale now that we should be able to get more efficiencies as we move forward.

Rob Sedran – CIBC World Markets - Analyst

I'm convinced this little clock runs fast, by the way. That's a half-hour. So thank you very much, Bharat.

Bharat Masrani – TD Bank Group - Group Head, U.S. P&C Banking

Where is the clock, by the way?

Rob Sedran – CIBC World Markets - Analyst

It's that little timer down there. We are actually 2 minutes over. Thank you very much for participating in the conference this year. It was great.

Bharat Masrani – TD Bank Group - Group Head, U.S. P&C Banking

Thank you, thank you very much.