TD BANK GROUP
SCOTIABANK FINANCIALS SUMMIT
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PARTICIPANTS

Bharat Masrani
TD Bank Group – Chief Operating Officer

Sumit Malhotra
Scotiabank – Analyst

PRESENTATION

Sumit Malhotra – Scotiabank – Analyst

Our next presenter this morning will be Mr. Bharat Masrani, Chief Operating Officer of the TD Bank Financial Group. Mr. Masrani has been with TD for the past 27 years in a number of progressively senior roles, including the Head of the U.S. Personal and Commercial Bank; Chief Risk Officer of TD Bank, as a whole; and senior roles in both corporate lending and TD Waterhouse. Mr. Masrani will be taking the President and CEO role over at the Bank on November 1.

And as he comes to the stage, I will point you – and you know what, since it's up here, I'll just point to the forward-looking statements and leave that for everybody else to read. Hello, sir.

Bharat Masrani – TD – Chief Operating Officer

Morning. How are you?

Sumit Malhotra – Scotiabank – Analyst

Good. How are you?

Bharat Masrani – TD – Chief Operating Officer

Good.

Sumit Malhotra – Scotiabank – Analyst

Thanks for your time.

Bharat Masrani – TD – Chief Operating Officer

Glad to be here.

Sumit Malhotra – Scotiabank – Analyst

So, I've been keeping this pretty consistent to get started.

Bharat Masrani – TD – Chief Operating Officer

Okay.

Sumit Malhotra – Scotiabank – Analyst

And as I've said a few times, we have a number of either new Chief Executives or soon to be new Chief Executives with us this morning. So, the question I wanted to ask you to lead it off, a little bit open ended, but give us a chance to hear your thoughts not only as a senior executive of the Bank but as a shareholder, like many of the people in this room, as you prepare to begin your tenure thinking about the medium term for TD, what are the areas of the business or the outlook that lead you to believe will be most challenging to continuing the strong growth track record the Bank has had, number one?

And then perhaps more interesting for you, what are the biggest opportunities that get you excited about being at the helm of this institution and also being a shareholder of the Bank?

Bharat Masrani – TD – Chief Operating Officer

Good to see you, Sumit, and good morning, all of you. I'd say that we have – my view, tremendous foundation as a Bank. We have a fantastic positioning in every business that we operate in. And frankly, one of the hallmarks of TD and why we've been so successful is that we are a very adaptable company. We are not as ideological as perhaps some others might be. Our view is that great companies adapt to the environment they find themselves in rather than hoping that the environment will change back to what it was. And TD is a great company. So, that's our strength. And every year, we face new headwinds and also many tailwinds. We are a diverse company that operates in largely North America, but we have businesses that span all aspects of financial services.

So, we have the foundation. That does not necessarily mean that there – the environment will continue to be what it has been previously. I mean, there are – I picked up some of the discussions you had earlier. I mean, there are headwinds out there. We are not living in a world where revenues are growing as fast as perhaps we've had previously. I think the economic environment has its own challenges. And that environment is different on both sides of the border where majority of our business resides. So, those are issues that we all worry about. I get paid to worry, but I couldn't be happier with the bank we have, the foundation we have. The strengths are unquestioned. That's my view. And there's no reason why TD will not continue to perform as we have seen.

You talked about what are the specific opportunities and challenges. Just to give you some specifics, there continues to be segments in our, say for example, Canadian business, where we think we still have more opportunity notwithstanding our overall size in the Canadian market. And we keep on working at it. Commercial banking is a good example in that regard. We identified credit cards as a key area a few years ago, and I think all of you know what we've done in that space, and I would say quite successfully. The U.S. is a particular growth area for us given the footprint we are in, our size and scale in that market. And as the U.S. gets out of, what I would call, the aftermath of the financial crisis, I think we are really well positioned.

Some of the headwinds would be more related to, given our balance sheet, interest rates matter, on both sides of the border. But at some point you assume that we get more normal in the rate cycle, and that I think is a great benefit to TD. But in the mean time, we have to manage through where we are. And frankly, we have and I'm very happy with how our team and our bank has performed during this low-rate environment.

Sumit Malhotra – Scotiabank – Analyst

Thank you for that. Let's start off directly with a business you know quite well, the U.S. personal and commercial bank. And this is maybe not necessarily an earnings issue but more of a bigger-term or a longer-term franchise issue. The model that TD has operated within the U.S., going back to the Commerce acquisition has been very customer-focused, convenience-focused, the WOW! factor, as the Bank has talked about.

However, there does seem to be a shift that's occurring from the branches or the stores, as TD calls them, into more of a, let's say, mobile payments, non-branch, channel-focused. Can you talk about how that affects the customer convenience proposition that the Bank has operated with and what does this mean from a potential cost perspective going forward to the TD U.S. franchise?

Bharat Masrani – TD – Chief Operating Officer

I mean without a doubt, the advent of these new channels is real. And frankly, I heard your earlier guest talk about the take-up on various digital platforms. And we're no different in that regard. But we firmly believe, we are a multi-channel company. And you may have heard this phrase before that we believe in making sure that we are available in the form that our customers want us to be and that by definition is convenience.

So, what we find is that our stores in the U.S. and branches in Canada play a central role in that. Our view is that our customers continue to value physical presence, but they also want convenience of other channels. So, we are balanced in that regard as you know, Sumit, in the U.S. that we continue to open new stores and at the same time, make sizeable investments in other platforms. Now, we do have our positioning. We are in the U.S., America's Most Convenient Bank. And that is important to us. That is a positioning that makes sense for us, that's allowed us to grow through the crisis. It has provided us with a platform that, my view would be, would be second to none.

So, it is a balanced approach. We do worry about how do you create the WOW! factor in newer channels. And I feel pretty happy as to what we are doing. So, one small example would be, like we were not the first bank in the U.S. to come out with taking a picture on your iPhone of your cheque and having it deposited. But what we did – and I'm not sure, like I guess I'm one of the older guys in the room – but I don't have steady hands. And if the check – if your hand moves a bit, it's going to reject. The Bank is going to reject it. So, our team thought about this that this is not really convenient.

Yeah, you might advertise you, you're out there doing that, but some of us struggle with finding that little icons and if I got to hit that perfectly and make sure I don't move, so that's multitasking, and some of us might struggle with that. So, our people came up with the idea, and I guess we're one of the few ones that does this, is you can touch anywhere on the screen and it will take a photograph of the check. So, we are adapting to these new channels and making sure that we continue to be America's Most Convenient Bank. And frankly, we are importing those approaches and techniques into our Canadian franchise as well. So I feel pretty good about that.

Another example might be ATMs. These were viewed as a dying breed not too long ago, but I feel particularly excited about that channel. We are – I think we might be the first bank, at least in Canada, that, I think, 100 of our machines now are image-enabled. And so how do we make sure that we provide that convenience where our customers instantly get a picture of the check they just deposited through the machine instead of guessing and hoping that whomever opens this envelope will find my check. So these are factors that are important for our customers, and we are making sure that not only are we adapting to it but providing that service.

Now your question on level of investment, there are markets in the U.S. where we still feel that we don't have enough physical presence. And we have made it – for example, a goal in New York City, we would like to be the third largest retail-focused bank in the city, and, making good progress, but that means opening new stores as well. So we are not doing our investment in other channels at the expense of giving up on physical locations because we think that's a central part of our customer need.

Sumit Malhotra – Scotiabank – Analyst

So, if I ask you to put on another one of your old hats of Chief Risk Officer, we'll combine a couple of things here. Just a couple of months ago, we heard from the OCC in the U.S. that in certain product categories, lending standards were becoming a little too loose for their liking, if you will. And if I combine that with the fact that a hallmark of TD during the Ed Clark era has been to be ahead of the curve on risk management and perhaps avoid some of the missteps that other banks have gotten themselves into. We're in that stage of cycle now where, I'll say it, U.S. banks aren't getting paid for beating on loan losses anymore. It's more about top line growth.

So, are you seeing some lending standards that make you somewhat uncomfortable? And is the U.S. bank backing away from lending in certain areas of the portfolio? What does that mean for the revenue outlook going forward, net interest margin notwithstanding or interest rates notwithstanding?

Bharat Masrani – TD – Chief Operating Officer

No doubt, you are at the stage of the recovery where loan growth becomes critical for all institutions. And as you would expect, generally, there is a widening of the risk curve, if that's the right phrase. I feel comfortable as to where we stand. To date, in the markets that we operate, I don't see a tremendous give-up in quality of the credits. I do see keen competition on pricing, but I don't see ridiculous terms that you would expect at some point in this cycle, so I feel comfortable as to where we are.

I think you are right to point out that TD takes risk management very seriously. We think when the whole world says credit risk is not an issue, we feel it probably is, and it has served us well. We're quite disciplined in that regard and feel good about it. We went through the crisis. I think we were a positive outlier from a U.S. perspective, and that has served us well. So, I don't see us participating in markets or industries or structures that do not fit our risk appetite. We've been very clear about that. And yeah, do I worry about it? Absolutely. I get paid to worry about these things. But I don't think we are at the leading edge of trying to do deals that don't make sense from a long-term perspective.

Sumit Malhotra – Scotiabank – Analyst

From a growth perspective, what area of the U.S. loan book do you feel best about because the Bank has had some cautious comments on mortgages via the refi, auto lending getting a little bit frothy? I think it's fair to say the issues with Target were somewhat unforeseen – well, were unforeseen when you got into that partnership. So, is it really the commercial portfolio that you see the best growth coming out of in the U.S.?

Bharat Masrani – TD – Chief Operating Officer

Not necessarily. I think, the credit card space is an example. I think there's more opportunity. If you look at our U.S. balance sheet, you'd say that we would be compared to our peers underweighted in that space.

We worked hard to build up a capability, and frankly, leveraging our customer relationship. So, one of the big opportunities we have in the U.S. is how do we deepen that relationship with our customers and how many products does every customer have through TD versus some other provider.

So, I think there's huge opportunities in what I would call traditional products. If you have a chequing account with TD, why would you not have a savings account? Why would you not think of TD as your first mortgage provider? If you want a bank card why would you not think of TD as your provider? So, I think there's lots of opportunities in the personal space for us. Now, that may not be the case for all institutions, but given where we are in our evolution, I think there's a huge opportunity.

We are busy building out our wealth capabilities in the U.S. private banking capabilities. And these are areas that are grossly underweighted from our perspective and underpenetrated, which I think is great because if we had been very good at customer-deepening relationships, then there will be limited upside, but I think for our bank there's huge upside.

On the commercial space, our model ensures that when we open a new store, for example, in New York City, we are just not focused on what is available from a retail perspective in that particular vicinity. For us, delivering the entire bank is a key part of what we believe in. And that is something that our bankers understand. It is something that is valued and rewarded frankly in the Bank.

So, I feel good that what I would call boring banking, one relationship at a time, one deposit dollar at a time, is what we are good at. It may not sound fashionable, and it does not create headlines, but that's what we do for a living.

Sumit Malhotra – Scotiabank – Analyst

One more on the U.S., and then we'll switch focus here. And maybe it's not even necessarily U.S. The recent acquisition activity of the Bank. First off, it's been quieter than we've heard from TD for a number of years. But on both sides of the border, in the U.S. we've had the Chrysler and the Target. In Canada, we had MBNA and then the Aeroplan partnership. So, it's clearly been more focused on books of business rather than the branch focus that was previously the case. And I think that strategy is clear.

When you think about the Target, financially it makes perfect sense. You're deposit rich, you're adding a high-yielding asset instead of having securities and treasury yields. But it would be more meaningful to the Bank from an ROE perspective if it was a TD Bank customer instead of a partnership. So, to what do you attribute the, somewhat, slow process the Bank has had in building out their own credit card capabilities in the U.S.? And is that something that we should see more of, rather than partnerships?

Bharat Masrani – TD – Chief Operating Officer

So, on the credit card space, in particular, we do have a two-pronged strategy with our U.S. franchise. We certainly have aspirations to become a major player on a bank card what I would call cards we would sell through our stores, making sure that if we have a mortgage customer, they have a TD credit card as well.

But at the same time, we do have, I would say, a credible strategy and presence in, what we will call retail card services, where we provide credit card products for certain types of merchants. I think Target is a good example of that. But that's not the only one we have. There's a few others we have in the U.S. And we think that is an important space to be. Unlike other markets, the U.S. is a little different in a sense that, that portion of the industry is not immaterial; it is very large and, frankly, very competitive, and it requires specific capabilities to be able to find partners that make sense, et cetera.

It is an important part of our strategy. I don't think you should be surprised, and frankly, I've been very open about this that if we were to get another Target-like deal, would we be interested? Absolutely, we would be. What's not to like? And that's a core part of what we want to do with our U.S. balance sheet. I mean, you made the point.

Arguably, we're one of the most liquid banks in the world from a U.S. perspective. And it will just makes sense for us because if there is one opportunity for us that we seriously work at day in and day out is that the asset side of our balance sheet in the U.S. And so, it makes a lot of sense. How are we doing on the bank card business? It's not one of those things where you can buy a portfolio and it looks great from day one.

Sumit Malhotra – Scotiabank – Analyst

Right.

Bharat Masrani – TD – Chief Operating Officer

Again, it's one customer at a time, our value proposition. And so, we worked hard with that. I think our suite of cards is as good as any. And frankly, we're seeing momentum from our U.S. franchise. And would I like more? Absolutely. Who doesn't? But it reminds me of the mortgage business in the U.S.

Four or five years ago when we put all these banks together, none of the legacy institutions had any capability of size or profile in the mortgage business. And we said, this is an important product. If you have a mortgage, then you're likely to have five other products and services with that customer. And if you don't, you have much less than that. So, it is an important product. It's becoming an anchor product. So, we went out and built the capability and making sure that we have the right product suite and frankly, the people who have confidence to sell this product through our various channels.

I think we've done reasonably well. I see a similar sort of story developing on the credit card space. We are – it's a huge opportunity for us. We are a very small player. We got 8-plus million customers in the U.S. So, it doesn't take a genius to figure out as to what penetration you need to have a very credible business, so we're working hard to get there.

Sumit Malhotra – Scotiabank – Analyst

I know the Dillard's portfolio just changed hands. GE has gone ahead with an IPO of their financial services business. Is it fair to say that credit cards remain the primary acquisition focus of the Bank and probably at this stage more so in the U.S. than anything else in Canada?

Bharat Masrani – TD – Chief Operating Officer

Look, from a Canadian perspective, was it four years or five years ago where we would have been one of the smaller players in the credit cards space?

Sumit Malhotra – Scotiabank – Analyst

And you lost the – remember, the Canada Trust, you couldn't keep the …

Bharat Masrani – TD – Chief Operating Officer

Right. We could not. We could not. And frankly, it was one of our focus areas and continues to be. Fast forward where we are today, we're very happy with where we are. And, we, without a doubt, like that space. I think given the size of our balance sheet, given the capabilities we have, that is an important asset class, but I wouldn't want you to be left with the impression that that is our only focus.

Sumit Malhotra – Scotiabank – Analyst

Okay.

Bharat Masrani – TD – Chief Operating Officer

There are opportunities in other asset classes that we don't think we penetrated enough of. We continue to be excited about the mortgage market in the U.S. Yes, we have done very well, but that's a huge market, and we feel that we can do more in that space in the U.S.

I think on the commercial side, from an asset perspective, we do have capabilities that are great for TD, for example, healthcare in the northeast of the United States. I would consider that as a core strength for our bank. And are there more opportunities in that space? I think so. I think given what's happening with the Affordable Care Act, that is getting clearer by the day, and that should open up more opportunities. So, I'd say organically, in the card space, or the mortgage space, or the commercial banking space, I feel pretty good that we do have the base from which we can grow.

Sumit Malhotra – Scotiabank – Analyst

This is just like a TD conference call, you – or Canadian P&C does $1.1 billion, leads the industry in growth, and we never talk about it. So...

Bharat Masrani – TD – Chief Operating Officer

Amazing, isn't it? We are 17 minutes or 27 minutes into it, and you haven't asked me...

Sumit Malhotra – Scotiabank – Analyst

I'll save the best for last here. So, obviously the Aeroplan portfolio has given a boost to the aggregate results, but at least on my math, the underlying business is still performing at the best levels of the industry. Maybe a two-parter here. First off, I think some of the revenue headwinds in the business are pretty well understood to the extent that those impact everybody, and the Bank certainly talked about NIM on the call.

Is there more that can be done on the expense side to keep earnings growth in Canadian P&C at the high levels of the industry? Number one.

And number two, one of your counterparts earlier this morning did talk about it in some detail. So, just given where the Bank is now situated in credit cards, do you feel that there are offsets in place or available to you for whatever is coming down the pipe on the Interchange side? And we can close on the Canadian P&C business there.

Bharat Masrani – TD – Chief Operating Officer

One of the key principles of the Bank has been to continue to invest for the future. We – crisis, no crisis, downturn, no downturn, we've been consistent that this is a key focus for us. And we've been consistent on this that the U.S., crisis or no crisis, we continue to build out stores because it is important for our franchise. And so, one of our – I mean we are not looking to compromise on that principle because of perhaps short-term pressures on financial performance. And so, I feel good that that has helped us a lot. And I talked about the ATMs, I talked about our digital sort of initiatives that are working very well. And so, yes, we will look at opportunities. I did signal in the call that we continue to spend money on finding productivity gains that makes sense for the Bank, and we continue to do that.

So, yes, without a doubt, there's always opportunities on the cost side. And we should – for sure, look for those, but it's not going to be at the expense of not investing for the future. So, that's a key part for us. I think your point on the Interchange space and all that, I mean, early days, yes, without a doubt, there's momentum that something will likely happen, but we are in business. We handle those issues as they come. And would I expect depending on what it is that the business model, the value proposition may be adjusted by various banks to make sure they adapt to the environment they find themselves in? I would think so.

I wouldn't want to speculate as to what happens there. But I think we are – of a size and scale and adaptable, where there's a new reality, we will make sure not only that our offerings are competitive, but they make sense from a financial perspective as well. The credit card space is relatively simple from that perspective. You've got your cost to supply the credit cards and you have cost of rewards, something will have to be adjusted depending on what comes out of it.

Sumit Malhotra – Scotiabank – Analyst

On that note, I want to thank you very much for your time.

Bharat Masrani – TD – Chief Operating Officer

Thanks very much, Sumit.

Sumit Malhotra – Scotiabank – Analyst

Pleasure. Thank you.