TD BANK GROUP
Q4 2018 EARNINGS CONFERENCE CALL
NOVEMBER 29, 2018

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Any forward-looking statements contained in this document represent the views of management only as of the date hereof and are presented for the purpose of assisting the Bank's shareholders and analysts in understanding the Bank's financial position, objectives and priorities, and anticipated financial performance as at and for the periods ended on the dates presented, and may not be appropriate for other purposes. The Bank does not undertake to update any forward-looking statements, whether written or oral, that may be made from time-to-time by or on its behalf, except as required under applicable securities legislation.

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PRESENTATION

Gillian Manning – TD – Head of Investor Relations

Thank you, operator. Thank you. Good afternoon, and welcome to TD Bank Group's fourth quarter 2018 investor presentation. My name is Gillian Manning, and I am the Head of Investor Relations at the bank. We will begin today's presentation with remarks from Bharat Masrani, the bank's CEO; after which Riaz Ahmed, the bank's CFO, will present our fourth quarter operating results. Ajai Bambawale, Chief Risk Officer, will then offer comments on credit quality, after which we will invite questions from prequalified analysts and investors on the phone. Also, present today to answer your questions are Teri Currie, Group Head, Canadian Personal Banking; Greg Braca, President and CEO, TD Bank, America's Most Convenient Bank; and Bob Dorrance, Group Head, Wholesale Banking. Please turn to slide 2.

At this time, I would like to caution our listeners that this presentation contains forward-looking statements, that there are risks that actual results could differ materially from what is discussed, and that certain material factors or assumptions were applied in making these forward-looking statements. Any forward-looking statements contained in this presentation represent the views of management and are presented for the purpose of assisting the bank's shareholders and analysts in understanding the bank's financial position, objectives and priorities, and anticipated financial performance. Forward-looking statements may not be appropriate for other purposes. I would also like to remind listeners that the bank uses non-GAAP financial measures to arrive at adjusted results to assess each of its businesses, and to measure overall bank performance. The bank believes that adjusted results provide readers with a better understanding of how management views the bank's performance. Bharat will be referring to adjusted results in his remarks. Additional information on items of note, the bank's reported results and factors and assumptions related to forward-looking information are all available in our 2018 MD&A and the fourth quarter 2018 earnings news release.

With that, let me turn the presentation over to Bharat.

Bharat Masrani – TD – Group President and CEO

Thank you, Gillian, and thank you, everyone, for joining us today. Q4 was a great quarter for TD, and it caps off a strong year for the bank. We executed well in all of our businesses guided by our long-term strategy as a purpose-driven organization operating from a position of strength as we build the better bank for tomorrow.

Here are a few key measures that underscore the quality of our results in 2018. Earnings surpassed $12 billion on a full-year basis, up 15% from last year's $10.6 billion, itself a high-water mark, and EPS rose 17% to $6.47. Revenue grew 8% and we achieved 400 basis points of operating leverage. Return on equity rose to nearly 17%, driven by increases in all of our business segments.

Our CET1 ratio increased 130 basis points to 12% including 20 million common shares bought back during the year. We also delivered good value for our shareholders. Our dividend paid increased by 11% on a full-year basis. We delivered above-average total shareholder return this fiscal year, and we led our Canadian peers for TSR over the 3, 5, and 10-year periods. And today, we announced our intention to repurchase up to an additional 20 million common shares for cancellation, subject to regulatory approval.

Let me now highlight some key accomplishments in each of our segments. Canadian Retail had a very successful year in 2018 with earnings up 10% surpassing $7 billion. Our banking, Wealth and Insurance businesses all performed well, as customers entrusted us with more of their business.

We strengthened our market leadership position in key product lines, maintaining our number-one ranking in credit cards, direct investing, and direct distribution and affinity insurance, taking share in private banking and extending our lead in personal non-term deposits, the bedrock of our high-quality balance sheet.

And we made further inroads across our other core products, continuing to take share in real estate and unsecured lending, and delivering another year of strong growth in business loans and deposits. We were also very pleased this week to announce a long-term agreement with Air Canada to become the primary credit card issuer for their new loyalty program when it launches in 2020. The agreement delivers stability, continuity and value for our TD Aeroplan customers, and reinforces our leadership position in the Canadian credit card business. The Canadian Retail business is winning with customers the way we always have – by putting them at the center of everything we do. That means working together as One TD, partnering across our business and functional teams to bring the whole bank to our customers.

We continue to invest in our best-in-class branch network, because our customers tell us it's important to them, and we're excited to take the next step with Future Ready, building on our leadership in comfort and convenience, Future Ready will see us elevate our advice proposition and equip our colleagues with the tools and training they need to help our customers move forward with greater confidence.

We're designing our digital capabilities the same way – by centering everything on the customer experience. And it's working. We have the #1 Canadian banking app, according to App Annie. We rank first in digital banking in Canada, according to Comscore, with the highest number of unique users, the strongest engagement, and the greatest reach. And the new sales tools we've added, like Easy Apply, are gaining similar recognition, with our chequing and savings mobile experience taking top spot in the latest Forrester survey.

Taken together, we have a compelling omni-channel strategy that's driving record high levels of customer acquisition and retention. Our focus on delivering personalized connected experiences to customers in their channel of choice is a winning approach and a key differentiator. It helped drive the strong results we saw in our flagship Canadian Retail franchise this year, and the business is well positioned for continued success in 2019.

Our U.S. Retail bank had a banner year in 2018, as strong growth across our businesses was amplified by the benefits of higher rates and U.S. tax reform. Earnings rose 23% to US$2.7 billion, an increase of more than $1 billion for the last five years. We achieved 300 basis points of operating leverage while continuing to invest in our businesses. And our efficiency ratio declined to the 55% range. With the contribution from TD Ameritrade doubling, segment earnings rose 33%. And segment return on equity reached nearly 13%, up 3 percentage points on a full-year basis.

Our U.S. Retail bank continued its strong momentum, building on our roots in Retail, small business and commercial banking, we have added capabilities and are building scale in auto finance, and corporate and specialty banking, Wealth and cards, allowing us to attract new customers and deepen relationships with existing ones. We have made significant investments to support this growth across all areas. We've optimized our store network, invested in frontline staff, introduced new digital capabilities, and continue to modernize our technology and data infrastructure to make banking simpler, faster, and more seamless for customers. Our U.S. Retail banking model is grounded in our people-centric culture and brought to life by our brand and community giving. It's a value proposition that is clearly resonating as we have continued to generate peer-leading loan and deposit growth and household acquisition. And it sets us up very well for 2019.

Rounding out our strong results this year, earnings in our Wholesale segment, again surpassed $1 billion and ROE climbed to 18%. We grew revenue in our capital markets business and we continue to win significant mandates globally and take market share.

We maintained our leadership position in the Canadian market occupying the number one or number two spot in key domestic rankings; equity and equity options block trading, debt trading, syndicated loans, M&A announced, equity underwriting, and government and corporate debt underwriting. TD Securities won an impressive range of advisory and lending mandates throughout the year. This quarter, we acted as sole financial adviser to George Weston on the acquisition of an additional 61.6% interest in Choice Properties REIT from Loblaw. We made significant progress building our U.S. dollar franchise with five years of continuous market share gains and a steady rise up the league tables. And we reinforced our credentials in the green and sustainability bond space, a growing segment of the market that is well-aligned with the bank's commitment to support the transition to the low carbon economy of the future.

Our Wholesale business continues to perform very well. We've strengthened our leadership in the Canadian market and we continue to expand our markets and banking business globally to meet the needs of our growing client base. We are winning increasingly complex mandates, thanks to investments in our capabilities and strong partnerships across the bank through our One TD strategy. It's an impressive track record of success. We feel good about our momentum, which we expect will continue in 2019.

Overall, it's been a tremendous year for TD. Our proven business model is a powerful enabler. The impressive results we've delivered reflect; a diversified business mix, our North American footprint, which offers growth and scale opportunities in a focused geography that helps us maintain our distinctive culture, and a risk appetite that has always served as our compass. The consistent earnings growth our model generates is a source of capital strength allowing us to make long-term investments in the customers, communities and colleagues who are at the center of our purpose-driven strategy; and in our commitment to shaping the future of banking to meet the demands of the digital age. We shared some of these highlights in our Annual Report. I invite you to read my message to shareholders in the pages that accompany it, which present our strategy in more detail as well as the purposeful investments it is enabling.

Now, let me conclude with a few thoughts on the year ahead. Our businesses enter 2019 with continued good momentum and a favorable backdrop. The Canadian and U.S. economies are performing well. We expect further margin expansion on the back of higher rates and credit quality remains positive. We have a proven business model with diversification and scale underpinned by a strong risk culture, strategic and differentiated advantages that have enabled TD to deliver consistent returns through the business cycle. Our view is that we can continue to deliver adjusted EPS growth in 2019 within our 7% to 10% medium-term target range. As you will appreciate though, we are watching market, macroeconomic and geopolitical uncertainty and there are current and emerging strains in the energy and automotive manufacturing sectors of the economy. If these factors intensify, they could impact our view of the year ahead.

To wrap up, I'm proud of what we achieved in 2018. We are focused on our strategy and executing effectively against it. It's a strategy that is deeply rooted in our unique and inclusive culture, and the sense of shared responsibility each of us feels to make the organization even stronger. I'd like to thank our more than 85,000 colleagues for their hard work and dedication to our vision, purpose and strategy. Our people are our greatest asset – they are what makes TD the better bank. I would also like to thank our customers for the trust and confidence they place in TD. I'm excited about the opportunities we have before us in 2019.

With that, I'll turn things over to Riaz.

Riaz Ahmed – TD – Group Head and CFO

Thank you, Bharat, and good afternoon, everybody. Please turn to slide 5. For 2018, the bank reported earnings of $11.3 billion and EPS of $6.01, up 8% and 9% respectively. Adjusted earnings were $12.2 billion and adjusted EPS was $6.47, up 15% and 17% for the year, respectively.

Revenue increased 7% with growth across all our business segments and expenses increased 4% on a reported and adjusted basis as we continue to invest in people and technology to execute on our strategy. Excluding the impact of FX, adjusted expenses increased 5%.

PCL increased 12%, primarily reflecting higher PCL in the U.S. Retail and Corporate segments, including higher provisions for the U.S. strategic cards portfolio, the partner share of which is held in the Corporate segment and offset in Corporate non-interest expenses. Canadian Retail and U.S. Retail delivered net income of $7.2 billion and $4.2 billion for the year respectively and Wholesale reported over $1 billion in earnings.

Please turn to slide 6. This quarter, the bank reported earnings of $3 billion and EPS of $1.58, adjusted EPS of $1.63 up 20%, reflecting strong results in all of our businesses. Revenue increased 9%. Provisions for credit losses increased 19% quarter-over-quarter, and expenses were up 11%.

Please turn to slide 7. Canadian Retail segment net income was $1.7 billion, up 5% year-over-year on good revenue growth, partially offset by higher expenses, insurance claims including CATs and PCL. Revenue increased 8% year-over-year, reflecting higher loan and deposit volumes, margin expansion, higher insurance revenues and wealth trading and asset growth.

Loans grew 6% year-over-year with increases in both personal and business volumes and deposits increased by 3% reflecting growth in business and personal deposits. Wealth assets grew 1%. Margin was 2.94%, up 1 basis point quarter-over-quarter primarily due to higher interest rates and partly offset by balance sheet mix. Net interest margin is up 8 basis points on a year-over-year basis.

Total PCL increased by 7% quarter-over-quarter, mainly reflecting higher impaired PCL. Total PCL as an annualized percentage of credit volume was 25 basis points, up 1 basis point quarter-over-quarter. Expenses increased 11% year-over-year reflecting higher marketing and promotion costs, higher employee related variable compensation in the Wealth businesses and increased spend on strategic initiatives.

Please turn to slide 8. U.S. Retail net income was US$855 million on a reported basis and US$874 million on an adjusted basis, up 34% year-over-year. U.S. Retail Bank earnings rose 26% year-over-year. The strong result reflects 8% revenue growth on higher deposit margins, loan and deposit volume growth, fee income growth and a lower corporate tax rate. Average loan volumes increased by 3% reflecting growth in the personal and business customer segments. Deposit growth was 5% including strong growth in core checking accounts of 7% and an 8% increase in sweep deposits from TD Ameritrade.

Net interest margin was 3.33%, flat on a quarter-over-quarter basis. Year-over-year net interest margin increased 15 basis points, driven by higher deposit margins. Total PCL increased 10% quarter-over-quarter, mainly reflecting higher impaired PCL. The U.S. Retail net PCL ratio including only the bank's contractual portion of credit losses in the strategic cards portfolio, was 50 basis points in the quarter, up 4 basis points from last quarter.

Expenses increased 3% on a year-over-year basis, reflecting higher investments in business initiatives, business volume growth and increased employee-related costs, partially offset by productivity savings. On an adjusted basis, expenses were up 5%. The contribution from our investment in TD Ameritrade increased by 111% year-over-year on a reported basis and 96% on an adjusted basis, adjusted for TD's share of charges related to the Scottrade acquisition. Segment ROE was 12.8% on a reported basis and 13% on an adjusted basis, up 330 basis points from a year ago. Please turn to slide 9.

Net income for Wholesale was $286 million, up 24%, reflecting higher revenue, partially offset by higher non-interest expenses, taxes and PCL. Revenue increased 32%, reflecting higher trading-related revenue and fee and advisory revenue. Total PCL was $8 million compared to a benefit of $14 million in the prior quarter. Non-interest expenses rose 28% reflecting higher variable compensation, higher initiatives spend, and continued investments in client-facing employees supporting the global expansion of Wholesale Banking's U.S. dollar strategy. Please turn to slide 10.

The Corporate segment reported a net loss of $181 million in the quarter compared to net income of $41 million in the same quarter last year. The increase in reported net loss was primarily attributable to the dilution gain on the Scottrade transaction in the same quarter last year and an increase in net corporate expenses partially offset by an increase in contribution from other items. Net corporate expenses were higher primarily due to the positive impact of tax adjustments in the fourth quarter of last year. Please turn to slide 11.

Our Common Equity Tier 1 ratio was 12% at the end of the fourth quarter, up 35 basis points from the third quarter. We had strong organic capital generation this quarter, which added 39 basis points to our capital position. Our leverage ratio was 4.2% and our liquidity coverage ratio was 129%. We announced our intention to amend our NCIB for up to an additional 20 million common shares, subject to regulatory approval.

I will now turn the call over to Ajai.

Ajai Bambawale – TD – Group Head and Chief Risk Officer

Thank you, Riaz, and good afternoon, everyone. Please turn to slide 12. The strong credit quality we saw throughout the year carried into the fourth quarter. Gross impaired loan formations were $1.4 billion or 21 basis points, up 3 basis points quarter-over-quarter and up 2 basis points year-over-year, reflecting new formations in the Canadian Commercial portfolio from which we anticipate immaterial credit losses and seasonal trends in the U.S. credit card and auto portfolios. Consistent with recent quarters, there were no new formations in the Wholesale segment. Please turn to slide 13.

Gross impaired loans ended the year at $3.15 billion or 47 basis points, up 2 basis points quarter-over-quarter and down 2 basis points year-over-year. The primary contributors to the quarter-over-quarter increase in gross impaired loans were: New formations in the Canadian Commercial portfolio, seasonal trends in the U.S. credit card portfolio and the impact of foreign exchange. The Wholesale segment maintained a zero impaired loan balance quarter-over-quarter. Please turn to slide 14.

Recall that our presentation reports PCL ratios, both gross and net, of the partner share of the U.S. strategic card credit losses. We remind you that the bank's contractual portion of credit losses is reported in the U.S. Retail segment whereas the partner share is reported in the Corporate segment. The bank's PCLs in the quarter was $675 million or 41 basis points, up 6 basis points quarter-over-quarter and up 2 basis points year-over-year. The primary factors contributing to the quarter-over-quarter PCL increase were: an increase in the Wholesale portfolio largely due to a prior period benefit, a one-time impact related to methodology enhancements in the Canadian RESL portfolio and seasonal trends in the U.S. credit card and auto portfolios. As experienced in previous years, PCLs typically rise in the fourth and first quarters in the U.S. credit card and auto portfolios due to back-to-school and holiday shopping. Volumes and delinquencies historically decrease in the second and third quarters as customers receive tax refunds and catch up with their payments. Please turn to slide 15.

Impaired PCL remained stable for the bank and the segments on both a quarter-over-quarter and year-over-year basis. Performing PCL increased $80 million quarter-over-quarter for the bank, reflected in the Corporate segment attributable to the U.S. strategic cards partner share and the Wholesale segment due largely to a prior quarter benefit. For 2018, the full year rate is 39 basis points, up 2 basis points from 2017 driven primarily by volume growth, seasoning and mix in the U.S. card and auto portfolios. Please turn to slide 16.

Given the recent decline in oil prices and widening price differentials, I'd now like to take a moment to discuss our oil and gas exposure. Drawn loans in the Producer and Services segment are $3.8 billion, representing less than 1% of total bank gross loans and acceptances. Of $3.8 billion, $600 million or 0.09% of total gross loans and acceptances is to producers exposed to Western Canadian Select, of which 83% is investment grade.

Excluding real estate secured lending, consumer lending and small business banking exposure to Alberta, Saskatchewan and Newfoundland and Labrador represents 2% of the bank's gross loans and acceptances. Overall, our underwriting standards remained consistent with those that saw us through the last price decline and we remain comfortable with portfolio quality.

Now moving back to total bank results, in summary, credit quality continues to be strong across the bank's portfolios and we remained well-positioned for continued growth going into 2019. Subject to quarterly seasonal fluctuations and provided economic conditions remain supportive, I expect fiscal 2019 PCL to be in the range of 40-45 basis points.

With that, operator, we are now ready to begin the Q&A session.

QUESTION AND ANSWER

Operator

Thank you. We'll take our first question from Gabriel Dechaine. Please go ahead.

Gabriel Dechaine – National Bank Financial – Analyst

Good afternoon. First question is on the Commercial real estate portfolio in Canada, and a couple of observations. One, you've been generating much lower growth than your peers have in that category. And then I do see some divergence though between what you call residential and non-residential whereby residential is growing fast and non-residential is actually going down. Just wondering, a) are you deliberately holding back growth in this category? And b) what's in the residential subcategories that might be causing that divergence?

Teri Currie – TD – Group Head, Canadian Personal Banking

So Gabriel, it's Teri. Thanks for the question. On the overall portfolio of Commercial real estate, you're right. The growth has been more muted versus the other areas of the commercial lending growth. I would say, if you look at our underwriting policies and approach through the cycle, we have, and Ajai just mentioned this, a very consistent approach through the cycle.

What we've seen in the marketplace is a pricing dynamic in some cases that we aren't willing to match from an economic standpoint and some covenants that don't meet our risk appetite. And so, taken in combination, we're making prudent decisions and walking away sometimes when it doesn't make sense. As it relates to residential versus non-residential, we would be sticking with core, high quality clients in the residential category, and as I said, just continuing to make prudent business decisions going forward.

Gabriel Dechaine – National Bank Financial – Analyst

Okay. Thank you for that. And I know we're in a bit of a rush here, but I want to sneak one in for the U.S. business. FDIC premiums are no longer deductible, I think in calendar 2019. Is that going to be having a big impact on your profit growth outlook for next year in that business?

Greg Braca – TD – Group Head, U.S. Retail

We look at a whole host of issues going into the New Year, and that is one aspect. And obviously, this was just announced and effective for 11/1 going into 2019. So we'll work through it, but we see this as a manageable item for the upcoming year.

Gabriel Dechaine – National Bank Financial – Analyst

All right. Thank you. Have a good day.

Operator

Thank you very much. We'll take our next question from Steve Theriault, Please go ahead, Steve.

Steve Theriault – Eight Capital – Analyst

Thanks very much. For Teri, there's obviously noise in the HELOC versus the mortgage line, but in aggregate, you look like you're continuing to take market share almost, 7% RESL growth this quarter. Can you talk about your outlook for next year? 2018's featured a lot of share growth, but looking ahead, do HELOCs start to normalize, come off the boil or do you think you still have more market share to gain in 2019?

Teri Currie – TD – Group Head, Canadian Personal Banking

Thanks, Steve. So we would continue to be looking at mid-single digit growth for our proprietary total real estate secured lending portfolio in 2019. The reason we feel comfortable with that – the reasons actually remain similar to what we've talked about in the past. As you'll recall with HELOC hybrid mortgage product, we've made many improvements to that product to make it a real mortgage substitute, a convenient and flexible option for the right customers. We're fourth in market share in that category. And so, the growth in originations we're seeing is about 90% to existing TD customers, and we're comfortable that we will continue to grow our business in that regard to customers who love us for their day-to-day banking and have borrowing needs or borrowing elsewhere.

In addition to that, we've continued to invest in our mobile mortgage specialists and have added just shy of 250 year-over-year. So they're an opportunity to meet our customers in their channel of choice. We've continued to invest in our Homeowner Journey end-to-end digital capabilities, and the preapproval capability that we launched just a few months ago has delivered strong preapproval volumes and is delivering good business as well. We've continued to invest in our credit operations center. So that's helping us to adjudicate loans more quickly and get customers to the answer they're looking for more quickly which meets their needs.

And then finally, we've been helping to train our people in our branches to ensure that our advisors are confident to meet our customers' needs. So in aggregate, with those investments, we do see the prospect of similar growth next year. What I would say is that there was some pull forward obviously with B-20 launched January of 2018. So we could see the rate of growth a little bit lower in the first half, but still looking at mid-single digits for the full year.

Steve Theriault – Eight Capital – Analyst

Okay. That's super helpful. If I could squeeze in one, just a quick one for Riaz; a bit of an odd one, but the professional advisory services line it's up like $100 million quarter-on-quarter and year-on-year. That's a pretty big number for advisory services. Is there anything outsized or anything you'd mention there?

Riaz Ahmed – TD – Group Head and CFO

Steve, I think it's mostly in relation to all the various initiatives that we have underway and the execution of those initiatives. So I think you should look at it in the context of continuing to just build our systems and capabilities out.

Steve Theriault – Eight Capital – Analyst

Okay. I may circle back. Thanks for that.

Operator

We'll take our next question from Sumit Malhotra. Please go ahead.

Sumit Malhotra – Scotia Capital – Analyst

Good afternoon. Maybe a couple of clarification questions to start numbers-wise for Riaz. Just on capital, from the level you're at right now, if I think about the items we know that are coming, Greystone, Aimia, and the RWA updates. Is 30 to 35 basis points an appropriate range for the impact of those three combined?

Riaz Ahmed – TD – Group Head and CFO

Yeah. I think Sumit that that would be a reasonable consideration. As you know, RWA growth can bounce around from time-to-time, but yes, about 30 basis points should be about right.

Sumit Malhotra – Scotia Capital – Analyst

Thanks for that. And then when you were going through your prepared comments for the U.S. segment, you mentioned the ROE which has moved up nicely this year. When I look at your supp-pack on page 6 – and I'll start by saying I know there's moving parts when we look at segmented returns on equity or returns on capital, but your equity base that you show us in that segment hasn't really changed much in the last couple of years even though, obviously you've been running new business, you've been increasing your earnings power. How does that get allocated? Because I would think equity would grow alongside what's happening in the business. And I apologize if this is something I should know and I've forgotten, but any help there would be appreciated.

Riaz Ahmed – TD – Group Head and CFO

Yeah. No, I think you're quite correct, Sumit, in pointing that out. But the allocation is based on required equity. And as our systems of risk measurement and risk-weighted asset measurement mature, you see some benefit of that accruing to that line. And so you're quite correct that it's been fairly stable, but you should think about it in the context that it's coincidentally stable and not that it doesn't reflect the appropriate volume growth.

Sumit Malhotra – Scotia Capital – Analyst

So even with RWA up $9-10 billion, year-over-year, the equity requirement in the business doesn't move alongside that?

Riaz Ahmed – TD – Group Head and CFO

Well because I think when the RWA grows, there are other factors in the calculation of capital that may offset it, Sumit. And so we can take you through that calculation, if you'd like to.

Sumit Malhotra – Scotia Capital – Analyst

All right. I maybe have something else, but I will now re-queue, give some others a chance. I'll come back. Thanks.

Operator

Thank you. We'll take the next question from Nigel D'Souza. Please go ahead.

Nigel D'Souza – Veritas Investment Research – Analyst

Good afternoon. Thank you. I just want to follow-up on gross impaired loans for the quarter end. Touching on the point you made on seasonality. So, I understand the seasonality effects in Q1, especially in credit cards from potential hangover related to holiday shopping and spending there, but could you kind of provide more color on what type of seasonal factors you see impacting autos and credit cards in Q4?

Ajai Bambawale – TD – Group Head and Chief Risk Officer

Sure. It's Ajai. So thanks for the question. So what actually occurs is right starting from the back-to-school period going up to the end of the holiday shopping season, you do see a build-up in volumes and you do see delinquency pressures because consumer wallets are stretched. So when you see the delinquency numbers go up, that attracts seasonally performing PCL and that continues to build, right I would say, in Q4 and Q1. Q1 tends to be the high-water mark. And then as customers get their tax refunds, in Q2, you start seeing that number come down. I would actually encourage you to go to the U.S. Retail PCL numbers, look at the last three quarters and look at the change between Q3, Q4 and Q1 each year. You'll see it there.

Nigel D'Souza – Veritas Investment Research – Analyst

Thank you. That color was very helpful. And if I could just sneak one last question in. When I look at the breakdown of impaired loans, and this is on page, I believe, page 20 of your supplement pack. There's $120 million build in your industrial construction and trade contractors bucket in Q4 relative to Q3. Could you speak to or just provide some more color on what exactly impacted that line item?

Ajai Bambawale – TD – Group Head and Chief Risk Officer

Yeah. So it's in that line item. I would call it, isolated, quite frankly, and from my perspective, it's well secured. I'd actually be very surprised to see any credit losses. So, you should think of it more of as isolated.

Nigel D'Souza – Veritas Investment Research – Analyst

Okay. Got it. That was very helpful. Thank you.

Operator

Thank you. We'll take the next question from Mario Mendonca. Please go ahead.

Mario Mendonca – TD Securities – Analyst

Good afternoon. Ajai, just a sort of follow-up on that last question. You said it was well-secured that impairment. Is that fair to say that there have been no PCLs on that line item at all?

Ajai Bambawale – TD – Group Head and Chief Risk Officer

They're minimal PCLs, I'd say.

Mario Mendonca – TD Securities – Analyst

And your rationale?

Ajai Bambawale – TD – Group Head and Chief Risk Officer

Well, it's well secured, isolated and it's very, very nominal, and I'll leave it at that, quite frankly.

Mario Mendonca – TD Securities – Analyst

And you see no trends that you would highlight in any other loans in that category then, that's specific to that one.

Ajai Bambawale – TD – Group Head and Chief Risk Officer

I don't, and that's why the use of the word isolated.

Mario Mendonca – TD Securities – Analyst

Okay. One follow-up and this is more of a general question that I've asked a few banks. On page 30 of your supplement, you refer specifically to – you offer some pretty good detail on the PCL ratios in various categories. And specifically in business and government, the PCL ratio is only 3 basis points, and that's been true for your bank, and frankly all the banks now for some time. Can you help me think through like what is a – and average is always a tough word, but what do you think is a normal level of PCLs for business loans for TD or a bank generally in Canada?

Ajai Bambawale – TD – Group Head and Chief Risk Officer

Yes. So, I think the PCLs had been in single digits. I would say probably in the 10 basis point to 15 basis point range. Again, we've been in a very, very benign environment for a long time. And I think over a period of time, you'll see some normalization. But again, from what I'm seeing there's nothing on the horizon. Our portfolio quality is pretty strong right now and as Bharat said, the economic outlook continues to be reasonable as well. But as the cycle changes, some normalization of credit in Commercial will occur.

Mario Mendonca – TD Securities – Analyst

And when you offer that outlook of say, I think you said 40 to 45 basis points for 2019, what number is in your mind or the back of your mind for the business loans, is it something like 10 basis points, is that reasonable to get you to the 40 to 45 basis points?

Ajai Bambawale – TD – Group Head and Chief Risk Officer

I don't have that detail available. But I'll tell you like in the 40 to 45 basis points, I have assumed some normalization of Commercial credit in Canada, some normalization of Commercial credit in the United States and certainly some normalization of Commercial credit or Wholesale credit in the dealer.

Mario Mendonca – TD Securities – Analyst

Okay. Thank you.

Operator

Thank you. We'll take the next question from Sohrab Movahedi. Please go ahead.

Sohrab Movahedi – BMO Capital Markets – Analyst

Hey, guys. I just wanted to ask a couple of questions. On the on the U.S. segment, the U.S. loan growth kind of continues to be in that low-single digit. Talk us through a little bit on what's the outlook for that.

Greg Braca – TD – Group Head, U.S. Retail

Sohrab, thank you for the question. As we've been talking for the last several quarters now, we've been saying very directly at these quarterly calls that more moderate loan growth would be expected across a number of portfolios. I think as we've come into more of our size in some of our Commercial, and corporate, and specialty portfolios, that would have naturally brought down the growth rate you've seen from a few years ago, market conditions that we've been talking about, and there's certainly high demand for quality paper out there amongst all of the banks. There's also other macroeconomic factors, a slowdown in M&A, and customers, and many of our commercial and corporate clients are quite flushed with cash on their own balance sheets these days.

On the consumer side, it's also been more moderate. I think you would have seen many of the U.S. banks calling down home equity and mortgage rates as the refinance boom has slowed especially given a rising rate environment. That said, I would just say that for our business in the U.S., we still believe that we can continue to take share. And while this number, on any given quarter will bump around a bit, we continue to believe we will remain an outlier in growth. And while 3% growth is a little bit more muted, as I said at the upfront, it continues, especially amongst our peer banks in the U.S. and larger banks continue to put us at the top of the pack.

If you look at some of the quarter-over-quarter numbers of Q3 to Q4, you would have seen a decent growth from Q3 to Q4, and I think this does bode well going into the New Year. But all things being equal, we think we will continue to take share on both personal loans and commercial loans going forward.

Sohrab Movahedi – BMO Capital Markets – Analyst

Okay. Thank you. Ajai, did you disclose the oil and gas exposure because you're worried about it or just because you thought we would be asking about it?

Ajai Bambawale – TD – Group Head and Chief Risk Officer

I think it's topical so I disclosed it. Quite frankly, I'm not worried about it because our quality is very, very good. And as you saw in the slide and I highlighted the impaired levels, quite frankly, they are negligible. So we are not seeing any quality issues, either on the non-retail side, and even Retail so far is pretty strong. But it's topical and I thought it was appropriate to highlight it.

Sohrab Movahedi – BMO Capital Markets – Analyst

Understood. And maybe if I can just sneak one in for Teri as well. Maybe it's a better conversation, Teri, for next quarter. But given the Aeroplan announcement, I was a little bit perplexed that after as many credit card transactions that the bank has done over the years, there is still a need to call out charges related to systems that you think you're going to have to take over the next couple of years. Can you elaborate on that right now, or is it better we wait until next quarter?

Teri Currie – TD – Group Head, Canadian Personal Banking

I'm happy to elaborate on it. So, we're delighted to be in the position as Bharat said to have been able to announce this long-term partnership and to be the primary credit card issuer for the Air Canada loyalty program. Aeroplan has been the premier loyalty program in Canada and we are very excited about the offering with Air Canada going forward.

As we work through the partnership and launching value for both current and prospective cardholders over the next couple of years, we did identify about $100 million in investment. That will be launching some new cards in the lineup. It will be rebranding for the new value proposition and lining up to the offers available going forward. It will also be enhancing some digital and channel capabilities with the opportunity to interact in Air Canada channels. And that will allow us to provide for cardholders a more personalized experience and offers that are relevant to their travel preferences. And some of these investments will be able to be leveraged more broadly in our Visa portfolio.

So when we take a look at what we will be delivering for Canadians and for our current cardholders and the cost of that versus the benefits to our business and the customers, we feel very comfortable with that tradeoff.

Sohrab Movahedi – BMO Capital Markets – Analyst

But is some of that marketing spend?

Teri Currie – TD – Group Head, Canadian Personal Banking

This would be more branding and launch activities than marketing spend.

Sohrab Movahedi – BMO Capital Markets – Analyst

Okay. All right. I think of them both as the same thing. Thank you.

Teri Currie – TD – Group Head, Canadian Personal Banking

But maybe the way to say it is, the cards will need to be rebranded to Air Canada cards.

Sohrab Movahedi – BMO Capital Markets – Analyst

Understood. Thank you.

Operator

Thank you. We'll take the next question from Darko Mihelic. Please go ahead.

Darko Mihelic – RBC Capital Markets – Analyst

Hi, thank-you. Just a couple of questions. The first is just wanted to verify the balance in trading from last quarter, is it just a reverse of what happened last quarter? And I think you guys were musing about changing your accounting for trading. Has that occurred? I didn't quite catch it.

Bob Dorrance – TD – Group Head, Wholesale Banking

Hi Darko, It's Bob. There was a modest reversal of what occurred in terms of mark-to-market of the trading deposits in Q3, which was outsized. So, there was some benefit in in Q4. And I think we've said that for the year that line item was de minimis for the year, but there was unfortunately volatility in Q3. And we are moving to account for that line item or those mark-to-markets through the fair value OCI convention. That starts in this quarter. So, it will reduce volatility once the whole book gets remarked in that fashion. In the interim, the outstanding book though, however, will still be going to P&L.

And I think, really, when you look at the trading revenue quarter in the last number of years, the quarterly range has averaged around $425-450 million, but there is volatility in trading revenue. So, this quarter was modestly ahead of what the averages have been but meaningfully ahead of both the previous quarter and a year ago's quarter. Both of those quarters were weak quarters. Hence the large increase. It's not a large increase relative to the average, but it's a large increase relative to two weak quarters, and that we're the comparatives.

Darko Mihelic – RBC Capital Markets – Analyst

That's helpful. So presumably some of the volatility of trading revenues though should decline on a go-forward basis under the new accounting approach?

Bob Dorrance – TD – Group Head, Wholesale Banking

Yes. The volatility related thereto are related to the market and the trading deposits will now go through OCI. So that will come out. Yeah. I think we've always felt that there's inherent volatility in trading revenues caused by markets as well as positions and the combination of the two. So I think when you look at on an annual basis, there's a reasonable amount of stability. But the intra-periods are volatile as you noted.

Darko Mihelic – RBC Capital Markets – Analyst

Thank you for that. If I could just turn to the U.S. Retail segment just for a discussion I suppose on the outlook for the net interest margin. And maybe you can help me understand, sometimes in the – we get annual disclosures, and sometimes things pop out at me that look a little bit peculiar and the one thing that really popped out for me in the Annual Report was when I looked at the cost of your U.S. business deposits, it looks like they almost doubled year-over year, and went from 211 basis points to 490 basis points. And I'm just wondering if that was an anomaly and if that maybe slowed down the NIM expansion, and maybe looking forward we should expect – well, maybe I'll just leave it there and maybe you can let me know if the forward NIM outlook for the U.S. is maybe more robust than what we saw in 2018.

Greg Braca – TD – Group Head, U.S. Retail

Darko, it's Greg and thanks for the question. So first, I should probably level set that as we'll talk here quarter-after-quarter. Any given quarter, the NIM, given so many inputs into that equation, will bump around. And if I just take you back to the comparison from Q2 to Q3, we were up quite healthily 10 basis points quarter-over-quarter.

And in Q4 on a Q-over-Q basis, it was flat and I would primarily signal that it was mostly because of mix even though we had one rate hike halfway through Q4. I would just provide maybe just a little bit of a view in that in Q1 we would expect another increase in our net interest margin just from the basis of what we have rolling off in our investment portfolio and the on-off rate versus old investments versus where the market is today. So I'd say that we would expect further NIM expansion in Q1.

Riaz Ahmed – TD – Group Head and CFO

I think, Darko. I'd just add to that. I think the table that you're looking at is specifically the business and government U.S. line where as interest rates come up, betas in business and government deposits tends to get little higher.

Greg Braca – TD – Group Head, U.S. Retail

And maybe I would just add a little on the betas, Riaz and Darko. We watch this very, very closely and we get asked the question, well, excluding sweeps, deposit rates are a little slower than we would have seen in the past few years. We're 4% up year-over-year. Still quite healthy comparison against most of our peers, are in the 0% to very low single digits. We continue to take share, but I'll go to the quality story, especially at this part of the rate cycle.

And if you look at our consumer DDA balances, those consumer balances are up 7% year-over-year, small business checking account balances are up over 5% year-over-year. And so the headline number for growth is one thing, but we're also paying very close attention to the whole beta conversation and it should be also a lens of quality of growth and not just chasing hot deposits.

Darko Mihelic – RBC Capital Markets – Analyst

Thank you. I guess what I was getting at was the deposit beta just seemed overtly high on the business side, and I was just wondering if that would, I guess it didn't impact the overall margin as much as I thought it would. So we can take that question offline if at all possible. I just want to do more follow up on that.

Greg Braca – TD – Group Head, U.S. Retail

I'd be happy to do it, because I would generally say that our betas are well within our peer range across interest-bearing and non-interest-bearing products, and we can certainly follow up on that.

Darko Mihelic – RBC Capital Markets – Analyst

Okay. Thanks very much.

Operator

Thank you. We'll take the next question from Meny Grauman. Please go ahead.

Meny Grauman – Cormark Securities – Analyst

Hi, good afternoon. A question from the Annual Report, your macroeconomic variables in the scenario analysis, oil prices seem to be conspicuously missing from there. So I'm just wondering, I guess you have a wide range of variables to choose from, but is there anything in that that you don't feel it is as important a variable in your scenario analysis?

Ajai Bambawale – TD – Group Head and Chief Risk Officer

So it's Ajai. Let me answer that. So I think oil prices are important. But they're an input into our macroeconomic models. So to the extent they impact GDP or unemployment, they certainly drive our moderate results. So they are important but they're an input into the model.

Meny Grauman – Cormark Securities – Analyst

That's clear. And then if I can just ask about TD Ameritrade and the question really is, do you feel that this business is going to be a drag when it comes to 2019 just on a growth basis? You talked about just how strong the year was for this business in 2018 and I'm wondering how you're approaching the outlook for 2019. I know there's an element of market dependency but what's prudent here in terms of expectations?

Riaz Ahmed – TD – Group Head and CFO

Let me take that, Meny. As you know, through 2018 and as you can see in TD Ameritrade's own disclosures that there was a number of tailwinds that contributed to their performance. The non-recurring one would obviously be U.S. tax reform. But the ones that are more sustainable are the lift in interest rates as well as the additional customers and volumes that were made available via the Scottrade acquisition, but also a higher level of general trading activity in the market.

So, I think you can look at the guidance that TD Ameritrade gives in relation to its earnings and you'll conclude – you'll see that they continue to feel that there's still a fair bit of growth to go here.

Meny Grauman – Cormark Securities – Analyst

Thank you.

Operator

Thank you. We'll take the next question from Doug Young. Please go ahead.

Doug Young – Desjardins Capital Markets – Analyst

Hi, i'll try to keep this quick. Just back to the U.S. NIMs, I'm just hoping to get a little bit of color on your outlook, more in the context of mix shift versus deposit margins versus loan yields, and specifically on the loan yields side. Are you starting to see – because loan growth has been so slow, are you starting to see an increased competitive pressure and pressure on the loan yields yet or is that just non-existent at this point?

Greg Braca – TD – Group Head, U.S. Retail

No. I think, first, I'd say just on the commercial portfolios, it certainly has been very competitive in the markets for quality drawn paper across many segments and industries. And our view of this has been, first, we're going to have a lens from a risk appetite standpoint. And we're just not going to go out on the curve notwithstanding where we feel we might be late in the cycle, and we're going to be conservative in what we do.

And secondly, I would say that our view of growth – I'll go back to the quality story that I mentioned on deposits. We're going to grow from a credit quality standpoint and from a return standpoint and a relationship standpoint. And if we can't get it those ways we walk away from a lot of transactions every day. But notwithstanding that, we still think we can continue to outpace the growth of the market and we think we've got room to run.

On the consumer side, there is a dynamic going on. Refinances have been very slow. Most banks have got double-digit decline in home equity balances with a rising rate. And certainly we've been growing cards and auto a little quicker given we were subscale or relatively smaller players in those businesses over the last several years. And that's why we would – on the other side of it, we'd call out the increases in PCL given mix and the growing balances around those portfolios. So, that's been a focus area of growth and we think we're still doing it the right way for us.

Doug Young – Desjardins Capital Markets – Analyst

And just on the NIM outlook because most of the uptick really going to come on the deposit margin side, is that really – or is there a little bit of mix left in there to come through?

Greg Braca – TD – Group Head, U.S. Retail

Yeah. So for us, the way we would look at it, the loans are a spread business. And the way we would look at the deposit book of business is that's why we're so focused on quality growth is that we want DDAs and we don't want the hot money growth and we want deposits that can be invested longer term. And we do think all things being equal, in a rising rate environment, we're managing betas quite well and we think if rates continue to rise over 2019, the NIM should generally be higher.

Doug Young – Desjardins Capital Markets – Analyst

Okay. And then Bharat, it's a good problem to have; a 12% CET 1 ratio. Obviously, some of that comes back next quarter with some of the transactions being done. Everyone always talks about what's the minimum level of CET 1 ratio. But what's the maximum you're willing to take this up to. Why not be a little more aggressive on the buyback or at least put in a little bit more that you could be, have a little bit more tool on the buyback.

Bharat Masrani – TD – Group President and CEO

Doug, we've talked about the bank's capital framework, or how we think about capital, and I won't go through all the details.

But we have terrific opportunities to continue to invest in our businesses. We will look at M&A transactions if they make financial and risk sense to us and strategic sense to us. There are certain areas we've outlined that we would be quite interested in. And on top of that last year we announced the 20 million share buyback and we completed it, and we announced another one this quarter. So, I feel quite comfortable. We continue to apply a framework in a disciplined way, and if circumstances suggest that we should up our buyback, then we'll certainly consider it and that's how I'm looking at this, Doug. It's a consistent story from us, nothing different.

Doug Young – Desjardins Capital Markets – Analyst

Thank you.

Operator

Ladies and gentlemen, unfortunately, that's all the time for questions that we have today. And at this time, I would like to turn the conference back over to Mr. Bharat Masrani for closing remarks.

Bharat Masrani – TD – Group President and CEO

Thank you operator, and thank you to all of you for joining us this afternoon. Very happy with how the bank and the numbers the bank has delivered for the quarter, that caps off a great year at TD. I do want to take this opportunity to thank our dedicated and great employees around the world, 85,000 strong, who continue to deliver for all of our stakeholders including our shareholders. So, a big thank you from all of us here.

And as well for folks on the phone, it is that time of the year, in case we do not meet in the next few weeks, then I wish you the very best for the holidays and we'll see you in the New Year. Thank you.