TD BANK GROUP
Q2 2019 EARNINGS CONFERENCE CALL
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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.

CORPORATE PARTICIPANTS

Bharat Masrani
TD Bank Group – Group President and CEO

Riaz Ahmed
TD Bank Group – Group Head and CFO

Ajai Bambawale
TD Bank Group – Group Head and Chief Risk Officer

Greg Braca
TD Bank Group – President and CEO, TD Bank America's Most Convenient Bank

Teri Currie
TD Bank Group – Group Head, Canadian Personal Banking

Bob Dorrance
TD Bank Group – Group Head, Wholesale Banking

Gillian Manning
TD Bank Group – Head of Investor Relations

CONFERENCE CALL PARTICIPANTS

Sumit Malhotra
Scotia Capital – Analyst

Meny Grauman
Cormark Securities – Analyst

Ebrahim Poonawala
Bank of America Merrill Lynch – Analyst

Robert Sedran
CIBC World Markets – Analyst

Steve Theriault
Eight Capital – Analyst

Doug Young
Desjardins Capital Markets – Analyst

Gabriel Dechaine
National Bank Financial – Analyst

Nigel D'Souza
Veritas Investment Research – Analyst

Darko Mihelic
RBC Capital Markets – Analyst

Scott Chan
Canaccord Genuity Corporation– Analyst

Sohrab Movahedi
BMO Capital Markets – Analyst

PRESENTATION

Gillian Manning – TD – Head of Investor Relations

Thank you, operator. Good afternoon, and welcome to TD Bank Group's second quarter 2019 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 second 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.

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 Q2 2019 Report to Shareholders.

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, Q2 was a great quarter for TD. Earnings increased 7% to C$3.3 billion and EPS rose 8% to C$1.75 driven by record results in our Retail businesses and a rebound in Wholesale. We had good revenue growth in the quarter, credit quality remains sound, and we continue to invest in building the bank of the future.

Our CET1 ratio held steady at 12% including 5.5 million common shares bought back during the quarter. Given our robust capital base and consistent ability to generate organic capital, we announced our intention today to initiate a new NCIB for the repurchase of up to 20 million common shares for cancellation, subject to regulatory approval.

Overall, I'm pleased with our results this quarter. They reflect the benefits of our diversified business mix and North American scale, as well as our risk discipline. Our proven business model is a powerful enabler - allowing us to deliver on our purpose today as we reinvest in our competitive advantages to transform the bank for the digital age. This quarter:

- We took a decisive step forward with our enterprise cloud strategy. It's part of a broader effort to modernize our operations and put in place a state-of-the-art technology architecture, one that increases our agility and creates productivity savings we can reinvest in delivering better customer experiences.

- We participated in the launch of Verified.Me, a blockchain-enabled digital ID service designed to allow customers to verify their identity quickly and securely using personal information they can send or share from their bank with service providers of their choice. Verified.Me is an exciting new application of an emerging technology developed through a collaborative market-led approach that is putting Canada at the forefront of the global move to a digital ID.

- We also continue to support the development of Canada's AI ecosystem. On the heels of our acquisition of Layer 6 last year, we are seeding the next round of innovation with our foundational investment in Radical Ventures, an AI-focused venture capital fund. Canada has become a magnet for top AI talent globally, and we are seeing the same phenomenon at TD where the Layer 6 team has doubled in size over the past year, accelerating our ability to drive better business decisions and enhance the customer experience.

These investments are at the heart of our forward-focused strategy, and they're just a few examples of how we are continuously adapting and reinventing ourselves to deliver innovative experiences for our customers. We were delighted to be recognized for our efforts on that front this quarter with not one, not two, but three J.D. Power awards for customer service excellence.

- In Canada, TDCT won the award for highest customer satisfaction levels among the big five banks, ranking highest in overall satisfaction, convenience, and channel activities;

- And TD Auto Finance Canada ranked highest in dealer satisfaction among non-captive retail lenders for the second year in a row.

- And in the U.S., TD Bank, America's Most Convenient Bank, received the highest customer satisfaction with retail banking in the Southeast, according to the J.D. Power 2019 U.S. Retail Banking Study.

As I've often said, we don't design our strategy to win awards; we win awards because of how we execute on that strategy. It's a testament to the value of our omni-channel approach and the power of the One TD model. And none of it would be possible without our people and their relentless focus on doing more for our customers every day across the enterprise and in each of our businesses.

Let me turn to our business segments now. Canadian Retail delivered again in Q2 with earnings of C$1.9 billion, up 2%, as strong revenue growth was matched by continued high level of investment.

- In the Personal and Commercial bank, our J.D. Power wins are just one outcome of putting the customer at the center of everything we do. Another is the volume growth we continue to generate as customers respond to the investments we've made in our products, platforms, and advice capabilities by entrusting us with more of their business.

- We also saw strong net asset growth in our Wealth business as we leverage our scale to create new sources of value for our customers. from digital resources like TD Direct Investing's new GoalAssist tool which enables web broker clients to build personalized investment plans; to the new mortgage and private debt funds we launched for our private wealth clients, offering access to TD Greystone's expertise in alternative assets. We're delighted with the progress of the Greystone integration which is bringing together two first class investment teams with complementary capabilities and highly compatible cultures.

Turning to the U.S., our U.S. Retail Bank delivered impressive results this quarter as well, with earnings up 12% to US$753 million. The strong performance was driven by good revenue growth, reflecting higher deposit margins and volume growth and positive operating leverage. And with the contribution from TD Ameritrade up 27%, segment earnings rose to US$948 million, up 15% or 20% in Canadian dollars.

We've laid a strong foundation for future growth in our U.S. business. Over the past 10 years we've been rebuilding our core infrastructure and platforms, this quarter successfully converting our small business customers to our new digital next-generation platform. Our J.D. Power win is a strong endorsement of these continued investments and of our commitment to create experiences that respond to our customers' evolving needs.

Rounding out our businesses, Wholesale Banking bounced back from a tough first quarter. Earnings were C$221 million, reflecting higher levels of M&A and underwriting activity alongside continued investment in the global expansion of our U.S. dollar strategy. TD Securities also won several signature mandates.

- We advised Goldcorp on their US$12.5 billion merger with Newmont to create the world's leading gold company.

- We advised Brookfield Business Partners and CDPQ on their acquisition of Power Solutions from Johnson Controls and co-led Brookfield's dual-currency term loan B and high yield bond financings.

- In our Global Markets business, we were awarded our first euro benchmark mandate by KfW, the biggest SSA issuer in the euro market. The €5 billion deal is TD Securities' largest SSA bond underwriting to-date and marks a major milestone in the growth of our euro franchise.

- And we led TD Bank's highly successful €1.5 billion five-year senior debt issue, the first benchmark senior offering in the euro market from a Canadian bank of bail-inable securities.

As I reflect on the first half of the year, I'm pleased with our performance. It reflects continued momentum in our franchise businesses, good credit quality, and better conditions this quarter for market-based revenues.

Looking ahead, the macro environment remains fluid, trade and geopolitical tensions are heating up, and economic conditions remain mixed with several output indicators still soft while employment growth remains strong. As we move through the second half of the year, we will remain focused on our long-term strategy which has delivered consistent earnings growth over time and provided us with the capacity to invest in our purpose – to enrich the lives of our customers, colleagues, and communities.

This month we issued two reports demonstrating our commitment to this purpose –

- our Environmental, Social and Governance Report which presents TD's ESG scorecard for 2018;

- and our report on The Ready Commitment which outlines the impact of our corporate citizenship strategy in our four priority areas of environmental stewardship, financial security, connected communities, and better health.

I encourage you to read these reports which provide a wealth of information on the purposeful investments our strategy is enabling.

I also want to take a moment to focus on the spring flooding in Eastern Canada. These events have impacted thousands of people in multiple communities. We've taken steps to provide support including financial contributions to the Red Cross and through our branch network as well as through direct customer outreach to help those we serve cope with the challenges. We're also closely monitoring the fires in Western Canada and are in touch with the Red Cross to determine how best to support those affected. In these moments we want to be there for our customers, colleagues, and community.

To wrap up, we are delivering strong results today while laying a strong foundation for the future. That includes the new workspace we are creating at 160 Front Street West, a brand-new office tower in the heart of downtown Toronto. Our vision for the future of our workplaces is built around the goal of bringing our people and teams together in ways that promote collaboration and improve workflow, supported by investments in the right tools and resources. 160 Front Street is a key part of this initiative. It'll be a powerful complement to our flagship TD Centre and a best-in-class workplace for our people, our most important asset. I'll close by thanking them, our more than 85,000 colleagues around the world, for living our shared commitments each day and devoting themselves to being ready for our customers.

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

Riaz Ahmed – TD – Group Head and CFO

Thank you, Bharat. Good afternoon everyone and please turn to slide 7. This quarter, the bank reported earnings of C$3.2 billion and EPS of C$1.70. Adjusted earnings were C$3.3 billion and adjusted EPS was C$1.75. Revenue increased 8%, reflecting volume growth and higher margins in our Retail businesses as well as higher fee-based revenues. Provisions for credit losses decreased 26% quarter-over-quarter, primarily reflecting seasonal trends in the U.S. credit card and auto portfolios. Expenses increased 8%, reflecting continued investments in employees supporting business growth and strategic initiatives.

Please turn to slide 8. Canadian Retail net income was C$1.8 billion, up 1% year-over-year reflecting higher revenue partially offset by charges related to the Greystone acquisition as well as higher expenses, insurance claims, and credit losses. Adjusted net income increased 2%. Revenue increased 8%, reflecting volume growth, margin expansion, higher insurance and fee revenue, and the acquisition of Greystone. Average loans increased 6% year-over-year and average deposits increased 3%, reflecting growth in both personal and business volumes. Margin was 2.99%, up 5 basis points sequentially reflecting a refinement in revenue recognition assumptions in the auto finance portfolio and an increase in the prime-BA spread. Total PCL decreased 10% quarter-over-quarter with reductions in both impaired and performing PCLs. Total PCL as an annualized percentage of credit volume was 27 basis points, down 2 basis points quarter-over-quarter. Expenses increased 11%, reflecting higher spend supporting business growth including additional FTE and volume-related costs, charges related to Greystone, an increased investment in strategic initiatives including marketing and capability builds in data and digital technology.

Please turn to slide 9. U.S. Retail segment net income was US$948 million, up 23% year-over-year on a reported basis and 15% on an adjusted basis. U.S. Retail Bank reported earnings rose 14% on strong revenue growth of 6%. Average loan volumes increased 5% year-over-year, reflecting growth in the personal and business customer segments. Deposit volumes excluding the TD Ameritrade sweep deposits were up 4% including 5% growth in core consumer checking accounts. Net interest margin was 3.38%, down 4 basis points sequentially primarily due to seasonal increases in deposits. Net interest margin was up 15 basis points year-over-year, largely reflecting higher deposit margins. Total PCL including only the bank's contractual portion of credit losses in the strategic cards portfolio was C$170 million, down 26% sequentially reflecting lower provisions for the commercial portfolio and seasonal trends in the credit card and auto portfolios. The U.S. Retail net PCL ratio was 45 basis points, down 14 basis points from last quarter. Expenses decreased 2% year-over-year, reflecting the elimination of the FDIC surcharge, recovery of a legal provision this quarter, and charges associated with the Scottrade acquisition in the same quarter last year. The contribution from TD's investment in TD Ameritrade increased to US$195 million and segment ROE increased to 13.2%.

Please turn to slide 10. Net income for Wholesale rebounded sequentially to C$221 million, reflecting higher trading-related revenue and advisory and underwriting fees as market conditions improved. Net income was down C$46 million from the same quarter last year. Revenue was comparable with Q2 of last year but reflecting higher advisory and underwriting fees offset by lower trading-related revenue. Non-interest expenses increased 16%, reflecting continued investments in the global expansion of our U.S. dollar strategy and the impact of FX translation.

Please turn to slide 11. The corporate segment reported a net loss of C$161 million in the quarter compared to a net loss of C$163 million in the same quarter last year. Net corporate expenses were lower year-over-year, largely reflecting lower net pension expenses in the current quarter. Please turn to slide 12. Our Common Equity Tier 1 ratio was 12% at the end of the second quarter, consistent with the first quarter. We had strong organic capital generation this quarter which added 40 basis points to our capital position, and this was mostly offset by growth in RWA reflecting volume growth as well as the transition of our Canadian credit card portfolio to AIRB as well as the repurchase of common shares in the quarter. Our leverage ratio was 4.2% and our liquidity coverage ratio was 135%. We announced our intention to initiate a new NCIB for up to 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 13. Credit quality remained strong in the second quarter across all business segments as evidenced by reductions in gross impaired loan formations, gross impaired loans, and credit losses. Gross impaired loan formations were C$1.34 billion or 20 basis points, down 6 basis points quarter-over-quarter and up 2 basis points year-over-year. The quarter-over-quarter decrease in gross impaired loan formations reflects higher prior quarter formations in the U.S. commercial portfolio primarily attributable to the power and utility sector 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 14. Gross impaired loans ended the quarter at C$3.3 billion or 48 basis points, down 5 basis points quarter-over-quarter and stable year-over-year. The U.S. Retail segment was the primary contributor to the bank's C$238 million quarter-over-quarter decrease in gross impaired loans, reflecting a reclassification to performing for certain U.S. HELOC clients current with their payments and seasonal trends in the U.S. credit card portfolio. The Wholesale segment maintained a zero impaired loan balance quarter-over-quarter.

Please turn to slide 15. 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 credit losses recorded in the Corporate segment are fully absorbed by our partners and do not impact the bank's net income. The bank's PCLs for the quarter were C$636 million or 39 basis points, down 11 basis points quarter-over-quarter and up 3 basis points year-over-year. The C$219 million quarter-over-quarter PCL decrease was driven by typical seasonal trends in the U.S. credit card and auto portfolios and the Canadian consumer lending portfolios.

Please turn to slide 16. Both impaired and performing PCL decreased quarter-over-quarter, reflecting U.S. seasonal trends, as already mentioned; generally lower performing PCL across Canadian Retail; and higher prior quarter impaired PCL in the U.S. commercial portfolio, primarily attributable to the power and utilities sector.

In summary, credit quality was strong across the bank's portfolios and we remain well positioned for continued growth.

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

QUESTION AND ANSWER

Operator

The first question is from Sumit Malhotra with Scotia Capital. Please go ahead.

Sumit Malhotra – Scotia Capital – Analyst

Thanks. Good afternoon. First question is for Riaz on capital.

Riaz, one of your counterparts this morning talked to us about IFRS 16 and the impact that would have to start 2020. Just thinking about that for TD and especially with your larger branch footprint, are you able to give us an idea what you're expecting from a capital impact for that implementation?

Riaz Ahmed – TD – Group Head and CFO

We are working our way through the standard, Sumit. And as you can appreciate, there are some interpretational items that we need to work our way through and some choices that need to be made. So, we're not prepared to quantify what the impact would be. However, as you well know, when the right-of-use asset gets capitalized at the beginning of the next fiscal year, it will be risk-weighted and I assume, I'm expecting the impact to be very manageable.

Sumit Malhotra – Scotia Capital – Analyst

All right. So that's something, as you said, there are some choices to be made, we can revisit that later in the year?

Riaz Ahmed – TD – Group Head and CFO

Yes.

Sumit Malhotra – Scotia Capital – Analyst

I'll wrap up with a question on the Wholesale side. I think you communicated to us last quarter, revenue would stabilize. We've seen that here. I just want to focus on the expense side of the equation, and specifically the build-out that has been referenced a few times. When we look at the head count in this segment, it's up about 10% year-over-year and you've had a pretty steady climb over that period of time. Just maybe two questions here, if you can give us an idea how this expansion is going to trend. Is there a number you have in mind as to the amount of full-time complement that has to be added to get to the scale in Wholesale outside of Canada that you are looking for?

And then secondly, I hope I'm not putting you on the spot, but I didn't see this in the Annual Report. Approximately how much of your revenue in this segment is being generated outside of Canada if we use full-year numbers for 2018?

Bob Dorrance – TD – Group Head, Wholesale Banking

We have invested in building out both the global markets businesses as well as the corporate and investment banking business, particularly to grow U.S. dollar revenue, both in the U.S. region as well as in other parts of the world in which we operate. We have had a fairly aggressive build in people on the front office side in the last 2.5 years. We have added approximately 200 front office people, roughly half and half are split between global markets and corporate and investment banking. And then of course, you need to also invest in infrastructure and people and support and control, etcetera. So, it's been a relatively large investment for TD Securities.

We feel we're at a point now though where that will slow down fairly meaningfully. We're still looking to add a person here and there in some of the areas. But we now are more focused on achieving the revenue that we're making the investment for, and there is a J-curve in that. Some businesses are further along in the cycle, we've been working at them. Our SSA U.S. dollar business has been up and running now for a number of years. And we are at a market share there where we're in the top five banks in the U.S. dollar SSA space. In that business, now we're starting to add euro and sterling, but it's a fully invested business. Contrast that to prime services in the U.S., it's a couple of years old. The first part of that was investing in systems and policies and metrics and people, but that is now running and the focus there is adding the clients that we now need to make it a more profitable business. And we have probably more of the latter types than we do the SSA business. Bottom line, Sumit, is the growth in FTE will be relatively small on the front office side.

Riaz Ahmed – TD – Group Head and CFO

Sumit, it's Riaz. On the matter of geographic mix of the revenue, as you know, we make very careful choices about how we define segments. And I think you should look at TD Securities as an integrated global segment. Yes, we do make disclosures in the Annual Report about where the sources of revenue are, and that is more a legal entity reflection of the accumulation and aggregation of earnings. But when you have global centers for example from a trading perspective that are in London, Singapore, New York, Toronto, and you have funding sources that come from a variety of sources, the trading book really should be thought of more as an integrated business unit. I don't think it makes sense to break out the Wholesale results in that way.

Sumit Malhotra – Scotia Capital – Analyst

Yeah. I'll leave it here. I mean, obviously, some of the Canadian peers anyway who have expanded more into the U.S. in the Wholesale business have provided that information. And I think really what I'm getting at here is, as Bob has detailed, you've certainly added full time complement in the U.S., and it would be interesting to see how the revenue progression for that expense that you've made is trending, and I think that would be helpful to gauge. So, I hear you, but hopefully that's another one we can revisit going forward.

Riaz Ahmed – TD – Group Head and CFO

Okay. Thank you.

Meny Grauman – Cormark Securities – Analyst

Hi. Good afternoon. If I look at year-to-date, adjusted EPS growth, it is about 4%, so I'm wondering how confident you are that you can still get to the bottom end of your 7% to 10% range for 2019.

Bharat Masrani – TD – Group President and CEO

Meny, this is Bharat. Last quarter when we talked about this, we said there are a lot of headwinds and tailwinds. That has not changed. In my remarks upfront, I talked about some of the risks that we see out there. But overall, our medium-term target of hitting 7% to 10% earnings growth continues to be applicable from TD, and we'll try very hard, as I said last quarter, to try and get towards the bottom end of that range going forward.

Many Grauman – Cormark Securities – Analyst

Okay. So it's still realistic.

And then just in terms of expenses, what's the outlook? In the past, you've talked about sort of a slowdown in the second half of the year in terms of expense growth and a ramping up in operating leverage.

Can you update us on how you're thinking about expenses in the second half of the year and operating leverage?

Riaz Ahmed – TD – Group Head and CFO

Yeah. Absolutely, Meny. It's Riaz. As we said coming out of 2016 that we were making room to make investments, and then if you look at our expense growth coming into 2017 and 2018, you can see that steady ramp-up of expenses, and particularly in 2018 over the four quarters, we had an increasing expense profile which is now beginning to plateau out and we're seeing a more level set of expenses from a quarter-to-quarter basis. So what that means is that we have brought our expenses to a level where we feel that we're making the investments that we need to make and still driving out the right productivity, but it just turned out that the result of that is in the first half, you see a larger expense growth number which will moderate quite a lot in Q3 and Q4, but at comparable absolute expense spending levels.

Ebrahim Poonawala – BAML – Analyst

Good afternoon. I just wanted to clarify something to your previous statement on expenses. From what I recall, we saw a pretty meaningful ramp-up in the back-half of last year. So, was the point there that we should see pretty healthy operating leverage in the back-half of the year when we look at the third and fourth quarter?

Riaz Ahmed – TD – Group Head and CFO

Yeah. I think that's exactly right, Ebrahim, as our expense spending growth rate and investment growth rate will normalize or moderate in the second half, it should create better operating leverage. And as you know, we always strive to create operating leverage year after year after year, and so I do expect that you'll see much better metrics on that front.

Ebrahim Poonawala – BAML – Analyst

Got it. And I mean I just wanted to focus on the U.S. Retail margin. One in terms of – Riaz, if you can just talk about what you're seeing in terms of deposit pricing pressure, with the Fed on hold and your outlook for the margin? And, secondly, if you can talk about any actions you're taking to protect the margin if the Fed ends up cutting interest rates at some point over the next 12 months given sensitivity to your margin as well as sensitivity at Ameritrade to declining interest rates?

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

Ebrahim, thank you for the questions. It's Greg Braca. I would just first start on the margin question. If we think about the quarter-over-quarter, you saw we were down 4 basis points, but I would like to point out that year-over-year, we're still up a healthy 15 basis points. Generally, the way we would look at the sequential quarter-over-quarter little bit of a dip is – Riaz upfront mentioned some seasonal deposits, or we could talk about it in terms of mix of loan and deposit volumes in quarter-over-quarter, and that contributed to the decline. But the way I would think about it and I've talked about this for a couple of quarters now, is the quality of the deposit growth and what we're seeing in the U.S. is a very competitive and dynamic environment with both large and small organizations really looking to put on deposits and show some ability to grow. Some are going about it with core franchise growth and some are paying up for it. We clearly are not in that latter half camp and our betas remain very well in check and we've done a very good job growing core DDA and core checking account growth, and we've talked about that in the past as well. Core consumer checking account growth up year-over-year 5% is healthy household acquisition and goes to our whole model around primacy and convenience and all of the things that we talked extensively about.

To your second question, when you think about protecting that margin, if interest rates would go the other way or whatever the case may be, I do think it goes back to the way I answered this first question, is that our goal here regardless of the environment is to drive core household growth, not pay up for hot deposits, drive core checking account growth and we're seeing that across all of our lines of business, including small business and consumer. So that's how I'd answer that.

Ebrahim Poonawala – BAML – Analyst

So just a quick follow-up on that. So, the margin went down seasonally impacted because of deposit mix shift. Is the outlook that it should hold relative to 2Q levels, or do you expect incrementally more compression as the year progresses?

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

Yeah. So, the way we look at any quarter-over-quarter or the next few quarters out, these things are going to tend to bump around a bit. And very difficult, because in addition to just volume, there's a whole host of things that we always talk about that goes into it, long-term rates, investments, loan yields. So, there's a whole suite of things that would go into that margin story. But what I would generally say is with a stable outlook from the Fed and barring anything further dramatic on the long end, you generally tend to see, as a general statement over several quarters, fairly stable margins.

Robert Sedran – CIBC Capital Markets – Analyst

Thanks. Good afternoon. Riaz, I just wanted a quick clarification actually on the comment you made about the Canadian margin, which was the impact of I guess the change in revenue recognition around the auto finance book. Can you give a little more color and whether that is a one-time item on the revenue line that will fall away or if that was a recurring thing that will keep the margin at the level it got to?

Riaz Ahmed – TD – Group Head and CFO

Yeah. Rob, what that's about is that we're seeing faster prepayments in the auto book, which would therefore result in faster revenue recognitions. It wasn't a methodology, it's actually the underlying assumptions. And I think that as we continue to see those prepayments, we'll see faster revenue recognition along in that portfolio.

Robert Sedran – CIBC Capital Markets – Analyst

So as long as consumer behavior remains what consumer behavior has been, the margin is going to evolve from here as opposed to giving back 2 or 3 basis points?

Riaz Ahmed – TD – Group Head and CFO

Yeah. I don't think that it should have a big impact on margins going forward. It may just come off as things level off a little bit in our new assumptions. So similar to what Greg said about the U.S., I think the Canadian margins probably bump around a bit from here, but that would be an adjustment to assumptions that doesn't occur all the time.

Robert Sedran – CIBC Capital Markets – Analyst

And so, the rest of the margin trajectory from here is consistent with the prior guidance, a bit of a leak upwards I guess?

Riaz Ahmed – TD – Group Head and CFO

I think a slight bias upwards, but I would say, as Greg indicated, it's true in Canada as well that a lot can change in terms of product competition and consumer behavior. I think it's better to say that it will bump up and down a little bit here and there.

Steve Theriault – Eight Capital – Analyst

If we can go back to capital markets for a moment and focusing on expenses. So the last couple of quarters, the expense line has been about C$600 million plus or minus a few million. Should we think of it as a new run rate? And I look at year-on-year, the revenue line was identical, expenses were about C$80 million higher. How much of that C$80 million or so year-on-year increase is from the higher U.S. expenses as you build that out?

Bob Dorrance – TD – Group Head, Wholesale Banking

We're of the view that the C$600 million a quarter is something that we should probably be modeling in ourselves and the reason I'm hesitating is that there's also regulatory build and technology build, and Brexit build and some of that may be recurring and some may not be recurring. I think we certainly have been spending money on the EU-27 regulatory, we've been spending a lot of money on that type of activity. So that may slow down. I think what the real key though is that we need to grow revenue to make the return on the investment and if that is not occurring at the pace we need, then we need to reduce expenses as well. So, we are focused on both.

Steve Theriault – Eight Capital – Analyst

Do you have a base case on when you'd like to see that return on equity get back to sort of the high teen level in terms of sort of trying to gauge your level of patience with all that?

Bob Dorrance – TD – Group Head, Wholesale Banking

This quarter would be good! No, I mean, we still have an objective of making a ROE more in the 15% range, I think we've referred to in the last number of years. I think the high teens are a little bit of an era in the past, given what's going on in the business. So that's the focus. And we'd like to try to achieve that as quickly as we can.

Steve Theriault – Eight Capital – Analyst

Okay. Maybe one more for you then, after the volatility from last quarter, I'm curious if there was any action taken this quarter sort of in reaction to last quarter that may have mitigated any revenue upside for Q2 in what's proving to be a pretty strong capital markets quarter across the whole group here?

Bob Dorrance – TD – Group Head, Wholesale Banking

I don't think there was anything that we were doing last quarter that we've changed and we're doing this quarter that caused anything in the results, the U.S. markets were strong especially in the latter two months of this quarter, and our investments there really are what's going to cause a change in the mix and perhaps more stability in our revenues overall. So, it's that investment that certainly helped the quarter and markets felt bad, whereas in the previous quarter, the lack of market activity in both Canada and U.S. combined with the expense run rate as you spoke of certainly was a negative factor.

Doug Young – Desjardins Capital Markets – Analyst

Hi. Good afternoon. Just two quick ones. Riaz, just in U.S. Retail, I think there was a recovery of a legal provision. I just want to see if you can quantify that and just that, so I have this correct, but that was netted out of net non-interest expenses, is that correct?

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

It's Greg, Doug. So, the way we would talk about that is we're not going to put a number on that. And the way we think about expenses in general is if that item had not occurred, our expenses would have been up year-over-year and expenses in general would have been reflecting our continued investment in the business, but we wouldn't put an absolute number on that release.

Doug Young – Desjardins Capital Markets – Analyst

Would that mean NIX would have been up low single digits?

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

Well, as we've said all along we still would have had positive operating leverage. And if I think about this for the first half of the year, we had expenses up 6% and for the first half you're going to have these numbers from time to time in any given quarter. So, for the first half of the year our expense rate even with this item is running roughly 3%. And certainly, we've had positive operating leverage for the first half of the year.

Riaz Ahmed – TD – Group Head and CFO

Doug, if you just look at the trend of non-interest expenses over the last six quarters, I think you can assume that's a good trend.

Doug Young – Desjardins Capital Markets – Analyst

Okay, that's fair. And then just lastly CET1 capital generation. I guess I'm trying to get a sense of I think historically if we went back like 15 basis points to 20 basis points per quarter is typically what people have talked about, I think, maybe we've talked about in relation to TD. We're going into a different environment, there's been regulatory rule changes. Is that still a reasonable level to expect for TD or is there something to change that would cause that to be lower going forward? Thank you.

Riaz Ahmed – TD – Group Head and CFO

I think that if you look at Slide 12, you can see that the net income less dividends contributed 40 basis points and then of the RWA increases of 27 basis points, just a little bit less than half of that was devoted to the migration of the card portfolio from standardized to AIRB. So I think you can see in that the capital accretion continues to still be very strong even in a very fluid environment.

Doug Young – Desjardins Capital Markets – Analyst

And that I guess that move of that card portfolio to AIRB, I mean, that in and of itself is done and so that's one time. Is there anything else that's on the horizon that would be similar in such that if you move to AIRB would have a negative impact?

Riaz Ahmed – TD – Group Head and CFO

Well, really in our business mix, cards are one portfolio which, when they migrate to AIRB, the risk weights on them are higher than standardized. Typically, it's the other way around and, of course, you're well aware that our U.S. non-retail portfolio is in the process of migration to AIRB. But that should be a benefit.

Gabriel Dechaine – National Bank Financial – Analyst

Good afternoon. I want to talk first about the commercial book in Canada and it looks like you guys didn't have any credit noise there. No real losses out of the ordinary like we've seen from a few other banks this quarter and last, mind you. Outside of Europe in quarter performance, we have seen some issues, then the Bank of Canada is raising their own concerns about corporate indebtedness and then we've also got this massive growth in commercial and wholesale loans in Canada.

I'm just wondering what do you think about that growth, and what are you seeing differently than what the Bank of Canada may be concerned about. Why are you not concerned about credit quality and commercial lending in Canada, in general?

Ajai Bambawale – TD – Group Head and Chief Risk Officer

It's Ajai. I'll start with PCL, and then Teri will talk about growth. We're definitely seeing very low PCL and loss rates across the commercial book. And I would describe the quality as good, but that doesn't mean there's no migration. There is some migration occurring, and I would put it in the category of gradual normalization. So, not like it's not occurring at all. I can't speak to the peers and what their book is like, but certainly in our book I feel it's strong, it's performing well, but there is some normalization occurring. And if you actually go to some of the ECL tables and you look at Stage 2 ECLs, you'll see a bit of an uptick and especially if you look at business and government, so you'll see some migration there.

Gabriel Dechaine – National Bank Financial – Analyst

So, what is driving that?

Ajai Bambawale – TD – Group Head and Chief Risk Officer

I think we're late in the cycle. So, it's not abnormal to see some migration so late in the cycle. I can't pinpoint a single thing that's pointing that and it's not a single sector. But I would say it's broad, but it's still low dollars.

Teri Currie – TD – Group Head, Canadian Personal Banking

And then it's Teri. From a commercial growth perspective, I'd say we're very comfortable with the business that we're putting on the books. We're continuing to put bankers on the streets in markets where they're building great relationships. Business succession continues to be an opportunity for us. And I feel comfortable that, as Riaz was quoted earlier this morning, we're prudent lenders through the cycle. And so, we're very comfortable with the business growth that we're seeing and open for business going forward.

Gabriel Dechaine – National Bank Financial – Analyst

Well, Teri, while I have you at the mic, thought I'd ask something with a bit more of a positive spin. We've seen the housing market go from a source of intense concern last year in the wake of B-20 and start data was dipping lower and lower. And in the last few weeks or months, we've started seeing some good start data, some positive sales data coming out of the GTA and Montreal as well. And the industry seems to be, I guess, bottoming out in terms of mortgage growth, RESL, I'd say. I'm just wondering, if you're generally as optimistic as you were about this business a little while ago, or maybe if there's some additional optimism today in your growth outlook for RESL growth and the ancillary businesses?

Teri Currie – TD – Group Head, Canadian Personal Banking

We've been talking for quite a while now about a mid-single digit medium-term outlook for proprietary total Real Estate Secured Lending growth, and I feel very comfortable with that for this year and going forward. We've been investing as you know in this business more mobile mortgage specialists, more training for our branch advisors, a leading capability that is fully digital to apply for a mortgage online. We've got a position as we've talked about in the past, where we are a force in hybrid HELOC loan market share and we're continuing to be able to advance there with customers primarily who are already customers of TD. And retention is very strong as well. So, we continue to feel good about that guidance going forward.

Gabriel Dechaine – National Bank Financial – Analyst

Outside of what you're doing, is there anything in the macro that made you more positive?

Teri Currie – TD – Group Head, Canadian Personal Banking

Certainly we are seeing, as you mentioned, particularly in the GTA the kind of start of that spring lending season and some good trends. It really is a tale of the two halves of the country, if you will, being a little bit tougher in the West. Although I would say under C$1 million in Vancouver and condos is still a hotly contested market for purchasers. And then GTA in particular a little bit stronger. So, it's early days in the spring season but we're seeing some green shoots.

Nigel D'Souza – Veritas Investment Research – Analyst

Good afternoon. Thank you for taking my question. So, I had one on the loan volume side and I wanted to focus on your auto book. So if I look at the Canadian Retail segment, auto loans are relatively flat and in the U.S. they are down slightly quarter-over-quarter. You mentioned prepayment rates; so higher prepayment rates this quarter and just wondering if what we're seeing in Q2 here, is that just a one-off nonrecurring kind of trend or what is your outlook given that we are late cycle and autos tend to lead the cycle. What do you see auto finance volumes playing out for the rest of the year?

Riaz Ahmed – TD – Group Head and CFO

I think on the matter of the prepayment, Nigel, it's Riaz, I'll just say that the way we look at these from an accounting perspective is we sort of look at the trend over a period of time. So, I don't think you should interpret this as a one quarter trend. When we look at our revenue recognition policies, and this applies across a wide number of products whether it be mortgages, auto or even corporate, you always look at kind of prepayment trends over a longer period of time to see if you've got an appropriate assumption that is going into it. So, I don't think you should look at it as one quarter; as far as longer term trends go. I'll let Greg comment on the U.S. auto piece.

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

Sure. So, you are right, and it would have been similar to last quarter Nigel. if we looked at Q1 over Q1, we were really coming down to a relatively flat year-over-year numbers for the last couple of quarters. We have a view too that we are later in the cycle. We also want an appropriate return. We also want to manage relationships and volume. And versus just a couple of years ago, you would have seen us growing 8%, 9%, 10% year-over-year in auto. We think we have the right mix of the business that we've been positioning this as you know in the U.S. And I wouldn't be surprised if over the next few quarters you saw it bump around that this level maybe up a couple of points. But this is generally where we see ourselves for the foreseeable future.

Nigel D'Souza – Veritas Investment Research – Analyst

That's really good color. And I just have one last question on if I could turn to just credit losses and PCL in general. There's a step down in provisions for your Canadian Retail segment and although seasonality has benefited that quarter-over-quarter there was a larger step down in prior years. So, it's still fairly elevated, up as you noted nearly 30% year-over-year. So, I wonder if you could provide more color there. Is there anything at play here in terms of do you expect that to trend lower over the coming quarters and having another step down or what are you seeing just on either the performing or impaired side in Canadian Retail?

Ajai Bambawale – TD – Group Head and Chief Risk Officer

Yeah. So, I'll talk about the year-over-year, it's Ajai. So, we're kind of moving off very low numbers like if you look to Q2 2018, our number was 23 bps and the lowest we've had is 22 bps. We're really moving off those very low numbers into what I would consider a little more normalized numbers. And I think 27 bps still remains in a very acceptable range of 25 bps to 30 bps. But what I am seeing is, and I mentioned this earlier, a gradual normalization of credit losses across the various books in Canada. So, my expectation is that normalization will continue to occur at a gradual pace, unless the economy turns, I should clarify.

Darko Mihelic – RBC Capital Markets – Analyst

Hi. Thank you. I have two questions. One for Bob Dorrance and an obscure question that anybody can answer I hope, so first for Bob. You mentioned that you didn't really change anything in the quarter and that's cool. But, I guess the question I have is one of the things that has been changing for you is the way you account for your trading deposits and we've seen a bit more shift in the fair value through profit or loss. And of course, this quarter we see trading rebounds to C$411 million from C$251 million last quarter.

So, the question is sort of twofold. First, were there any marks from that that suppressed or helped the trading revenue or more importantly from my perspective is as we continue down this path of shifting the accounting regimen, will there be any sort of headwinds or tailwinds to trading revenue for the next couple of quarters?

Bob Dorrance – TD – Group Head, Wholesale Banking

There was nothing meaningful quarter-to-quarter, Darko, in that particular part of the business. I think as you look at I think Q3 last year was where we had called out for the first time that there was a meaningful reduction in revenue that occurred as a function of marking the trading deposits in the way that we were marking them. We have probably migrated roughly 50% of the book to fair value through OCI.[1] So it'll be a positive year-over-year but it won't be on a full amount.

Darko Mihelic – RBC Capital Markets – Analyst

Okay. So, in other words, just modest headwind or tailwind I suppose to trading revenue?

Bob Dorrance – TD – Group Head, Wholesale Banking

I would say that. Yeah.

Darko Mihelic – RBC Capital Markets – Analyst

Okay. Thank you. And then my obscure question. So, I appreciate the commentary that quarter-over-quarter and it looks as though the presentation in the way you designed it around credit quality, is that quarter-over-quarter we saw a bit of an improvement and there's less stage 1 and stage 2 less on performing, I suppose. But when I open up the supplementary capital, it's a different story. In Q1, asset quality helped your RWA. In this quarter, asset quality went the other way and you actually had to increase risk weighted assets because of asset quality movements. And the reason why I ask this is typically what we're concerned about in some thesis is that as provisions rise and as things get worse not only will your provisions for credit losses rise but so will your RWAs. And yet in two quarters, we have the opposite sort of phenomenon happening at TD. So, I'm wondering if you can maybe connect the dots for me, if at all.

Riaz Ahmed – TD – Group Head and CFO

Are you, Darko, looking at the flow statements for risk-weighted assets?

Darko Mihelic – RBC Capital Markets – Analyst

Yes.

Riaz Ahmed – TD – Group Head and CFO

Yeah. So, I think, as Ajai indicated earlier, that you can see a little bit of migration in the books, and so that you end up having – you can end up having an instance where both the PCLs and risk-weighted assets are experiencing the similar migration in that way because with the way Basel III and IFRS 9 works, you can

[1]Designated at fair value through profit or loss, with changes in fair value attributable to changes in the Bank's own credit risk recognized in Other Comprehensive Income (OCI). See Note 11 of the Q2/2019 Interim Consolidated Financial Statements for more information.

get a little bit of doubling up of your procyclicality. But, as we indicated earlier, that number you can see in the flow statements is not that significant, and so a gradual normalization is how we like to describe it.

Darko Mihelic – RBC Capital Markets – Analyst

So, when I look at it though, I mean for year-to-date, you have a 3.5% increase in your risk-weighted assets. And most of that would be just from portfolio from adding to the loan book. But, a portion of it is also because of credit quality. And I'm not singling out TD, it is much bigger at one of your peers. But again, it's just quarter-to-quarter I suppose, I guess what I'm getting from you is the answer is, they can go opposite ways. But over a period of time, I'm just trying to confirm that the general view would be that provisions for credit losses and RWA inflation for lack of a better word should go hand in hand.

Riaz Ahmed – TD – Group Head and CFO

It could. But, there are sometimes differences in how the two are looked at. For example, the calculation of expected shortfall in capital is different from how it's done for IFRS 9 purposes, so there can be methodology differences. And if you look at that asset quality line over the last five quarters, you can see it was up in Q2 of 2018, but it was down in Q3, down again in Q4, down again in Q1. So, I think your thesis that there is a general trend indicator here would not be evident in the numbers.

Ajai Bambawale – TD – Group Head and Chief Risk Officer

Let me just build on that. I mean, there's definitely some credit migration occurring, and that credit migration is going to be reflected in the RWA numbers. But if you really look at ACL, and if you look at ACL year-over-year and go and look at it by stage, okay, so total ACL is up C$333 million, and these are in the disclosures, year-over-year a big part of that is FX, but excluding that the increase in Stage 3 is actually very little, it's C$50 million. And then most of the increase is actually Stage 1, which I would describe as largely volume, but there's some mix in seasoning there, but there is a number for Stage 2 as well. And some of that is commercial migration, which will naturally show up in the RWA numbers, and there's mix in seasoning also occurring across some of the portfolios.

Scott Chan – Canaccord Genuity – Analyst

Hi. Good afternoon. lots of questions on the Canadian housing, but I wanted to switch to U.S. housing, and perhaps get your take on kind of what's unfolding there. And when I kind of look at your books, your residential mortgage is very solid and your HELOC book is trending downwards and maybe some thoughts regarding those portfolios for the balance of the year.

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

Sure, Scott, so first I would say, I'm glad you pointed it out, the mortgage book has been up for several quarters now year-over-year and we were up 8% this quarter. As you might know, if I just contrast this to just a few quarters ago or back before last year and the cycle of rate hikes really intensified. It would have been more of a balanced mix between refinance and purchase. And we've seen this certainly swing to a purchase market with far less on the refinance as rates have been moving up for the last year and a half.

The volume that we're seeing is decidedly being driven by jumbo mortgages and certainly not only into the consumer book but also into the private bank and in the wealth business in the U.S.

You correctly point out that the home equity business is down and we're down 6% year-over-year, but I would also contrast that to many of our peers and they're seeing double digits for quite some time now and that's just evident of when rates started going up, there's been a large refinance out of home equity into more permanent or fixed rate mortgages. And even we're seeing a little bit of an uptick with that with rates beginning to stabilize over the last three months or four months and actually come in in the long end, folks have had another bite at that apple on the refinance side for home equity balances.

Relative to peers, while we're down in home equity and it's certainly less than half of its sizable book than we are in the mortgage side, we are still seeing outperformance relative to peers even though we're down year-over-year.

Sohrab Movahedi – BMO Capital Markets – Analyst

Hey, thank you for that. Just two quickies. Teri, does your business do any lending to the private mortgage market?

Teri Currie – TD – Canadian Personal Banking

My business does not.

Sohrab Movahedi – BMO Capital Markets – Analyst

And so Ajai, is there a policy around any lending to mortgage investment corporations or otherwise at the bank?

Ajai Bambawale – TD – Group Head and Chief Risk Officer

I'm pretty confident there are policies and we limit any of that kind of lending.

Sohrab Movahedi – BMO Capital Markets – Analyst

Can you quantify it?

Ajai Bambawale – TD – Group Head and Chief Risk Officer

No, I don't have that information available.

Sohrab Movahedi – BMO Capital Markets – Analyst

Okay. And then just to go back to Darko's question. If you have negative migration and you are reflecting that negative migration through a higher provision whether it's Stage 1, Stage 2, or Stage 3. Will that then relieve some of the pressure that we would have otherwise expected to see from RWA appreciation?

Riaz Ahmed – TD – Group Head and CFO

Well, as I said Sohrab, it might to some extent, but the two systems don't really work hand in hand. The risk weighting system is different from the IFRS 9 accounting system. So, as I said earlier, you can get overlaps and that just increases the procyclicality of the regime. But, given the quality of the credit book in our underwriting, we wouldn't anticipate that it would give us big swings.

Sohrab Movahedi – BMO Capital Markets – Analyst

So, just to play that back to you, Riaz, maybe take another kick at it. If capital ultimately is intended to defend against unexpected losses and you therefore have expected deterioration in the credit quality and reflected through higher RWAs then presumably or through higher provisions, then presumably don't you need to also account for it through higher capital retention? Is that fair?

Riaz Ahmed – TD – Group Head and CFO

I think, in principle, that is the correct framework, Sohrab. And if you go back and look at all the comments that were made to the various authorities around the accounting provisions and the introduction of the various Basel rules, those provisions were pointed out. And I think those papers give you a pretty good understanding of how those two interact.

Bharat Masrani – TD – Group President and CEO

Thank you, operator. TD delivered a great quarter. And I want to take this opportunity to thank our 85,000 TD bankers around the world who are continuing to deliver for our shareholders. Thanks for joining us this afternoon and see you in 90 days.