TD Asset Management

Investor Knowledge 10 Minutes

Building a Healthy Portfolio

Gaining exposure to the Healthcare sector can help boost a portfolio's return and reduce volatility

At a Glance

- The Healthcare sector benefits from strong secular tailwinds including demographics and innovation. These trends are anticipated to remain in place for many years.
- To take advantage of these secular trends, investors can seek diversified exposure to the very broad-based Healthcare sector, and its many growing segments.
- TD Global Healthcare Leaders Index ETF (TDOC) can provide diversified healthcare exposure through a single one-stop solution.

Health is our greatest asset

Personal health is arguably our greatest asset. Good health provides us hope, opens doors to pursue our passions, and can allow us to enjoy the lifestyle we seek. Around the world, healthcare has largely been adopted as a human right, with governments, individuals, and corporations investing ever increasing amounts into providing healthcare.

For investors, Healthcare can be a highly attractive sector deserving of a core long-term position in many portfolios. The sector benefits from many attractive attributes, including strong growth and sticky demand for healthcare that is resilient to the ups and downs of the economy — a trend we, at TD Asset Management Inc., expect will continue in the years ahead.

Diagnosing the Healthcare sector's future

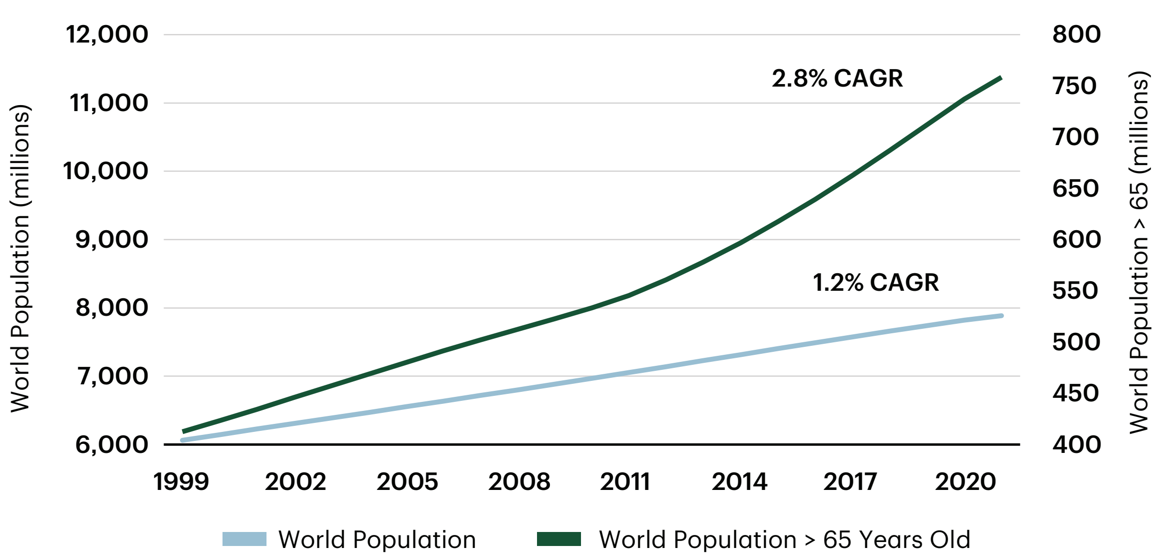
When we dig a bit deeper, it becomes clear that the strong growth in the Healthcare sector has and continues to be mainly driven by two secular drivers. This includes a growing and aging global population (demographics), as well as a continuous stream of innovations.

Growing and Aging Global Population + **Continued Innovation** = **Healthcare Sector Growth**

Demographic tailwinds will persist for many decades to come

Driven by a growing and aging global population, demographics is an important factor to the growth of the Healthcare sector. With the world's population continuing to grow, a deeper look into this growth can shed some light on this secular trend. While the world's population has grown at a compound annual growth rate (CAGR) of 1.2% over the past 20 years, the rate of growth for those 65 and older has been more than double, growing at 2.8% (as seen in the chart below). As a result, the world is getting grayer.

The world is getting grayer: annual global growth rates



Source: The World Bank, TD Asset Management Inc., as of Dec 31, 2021.

As an increasing share of the world's population ages, the demand for healthcare services will inevitably grow and, by extension, companies in the Healthcare sector will likely benefit from the greater demand. With demographics over the next few decades essentially all but written in stone, these tailwinds to the sector can be confidently viewed as durable and sustainable.

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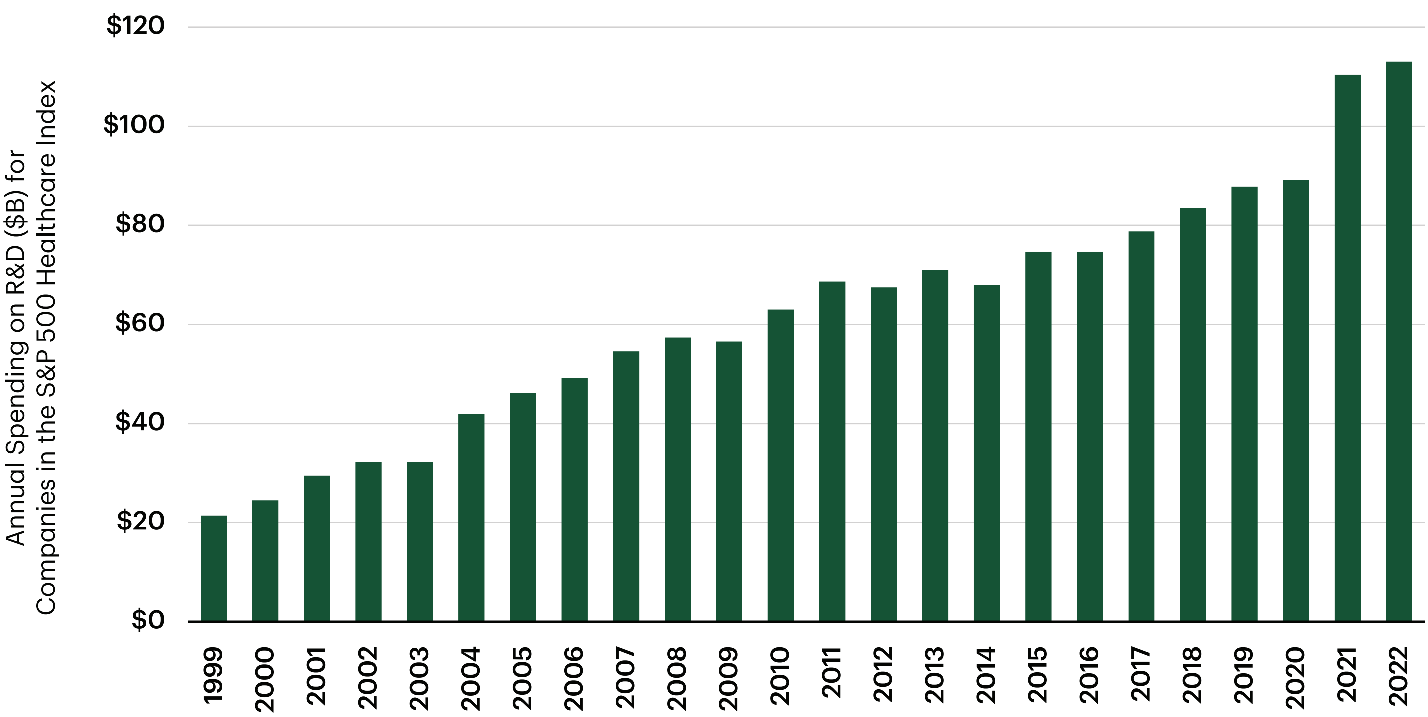
Innovation has been a huge driver of sector outperformance

While demographics has been a tailwind to sector growth, it only partially explains the strong outperformance of the sector over the long run. In fact, the bigger driver of outperformance over time has been innovation.

Innovation continues to expand what is possible in the field of healthcare, allowing us with time to treat, and provide better outcomes, for an increasing array of conditions over time. Moreover, given the high unmet need across a range of diseases, there remains plenty of runway for companies to continue to innovate in the decades ahead.

Looking forward, one promising indicator that suggests innovation will continue to remain strong has been the ever growing spending on research and development (R&D) by the Healthcare sector. By simply looking at the companies that make up the S&P 500 Healthcare Index, you can see this relentless growth. R&D spending for the group has gone from $22 billion per year at the turn of the century, to over $113 billion today, a 7% CAGR.

R&D spending continues to rise



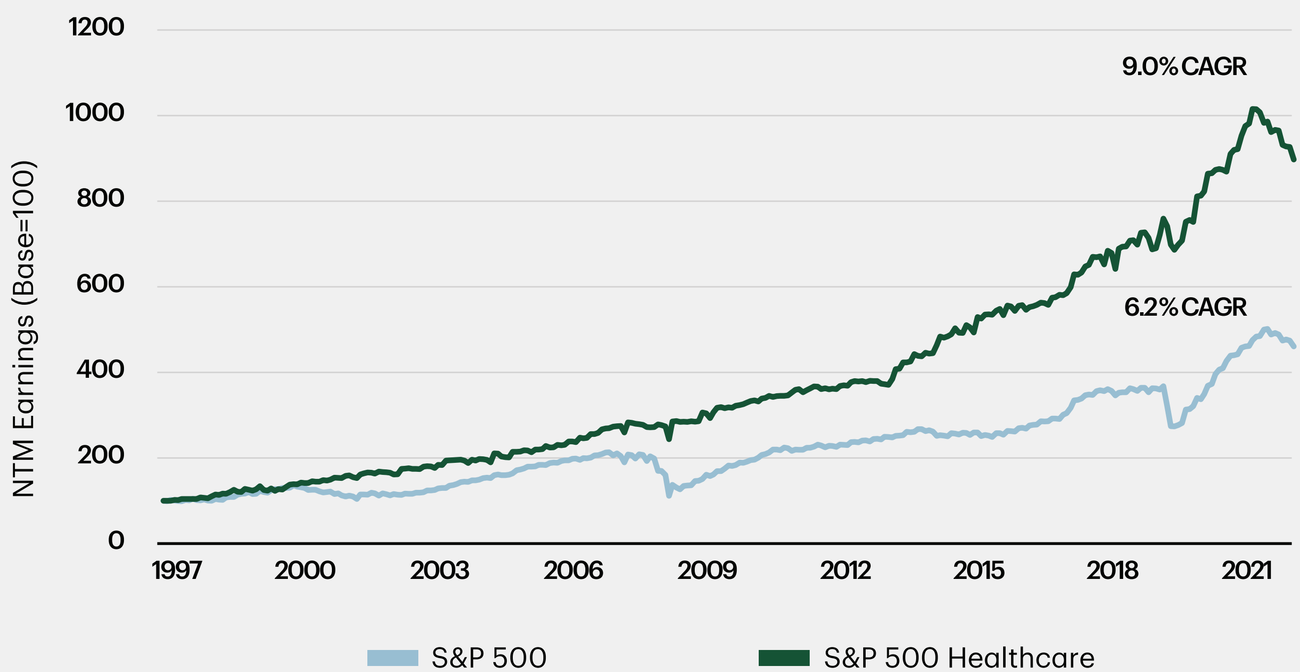
Source: TD Asset Management Inc., as of Dec 31, 2022.

Secular trends translate to equity market performance

When we put it all together — secular tailwinds from demographics, innovation and sticky demand for healthcare that is resilient to the ups and downs of the economy — Healthcare has been one of a few sectors which has exhibited above average earnings growth, but with less earnings volatility than the broader equity market.

All-in, the Healthcare sector has grown earnings at a 9.0% CAGR over the last 25 years vs 6.2% for the S&P 500 Index. Earnings drawdowns during recessions have typically been in the single digits.

Earnings growth of the Healthcare sector vs. the S&P 500 Index



Source: TD Asset Management Inc., As of January 31, 2023.

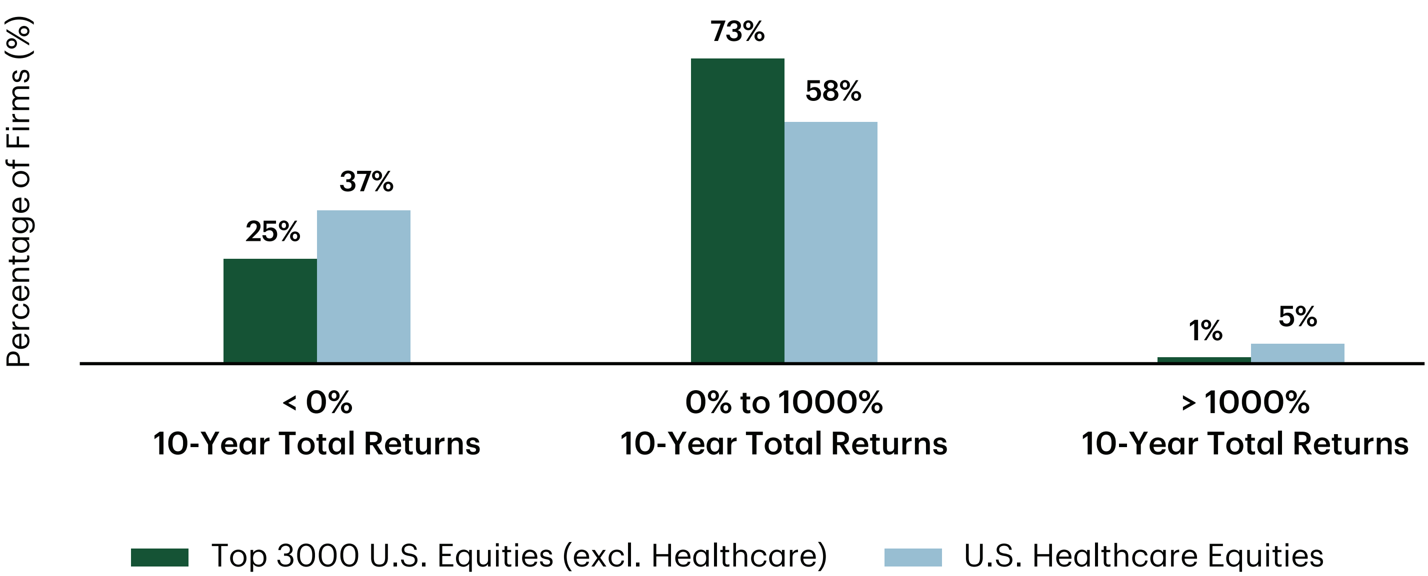
Broad exposure is key

While healthcare earnings on the whole have grown strongly and fairly consistently over several decades, there is a disparity between the winners and losers. For instance, in the Biotech segment, it is not uncommon for a stock to decline more than 50% when a drug fails clinical trial, while others can rise over 100% on a successful trial outcome.

Moreover, when looking at the performance of the top 3,000 U.S. stocks over the past 10 years when compared to the average performance of Healthcare equities, we also observe dispersion. For example, 37% of all Healthcare stocks generated negative returns over the past decade compared to 25% of non-healthcare stock. However, 5% of Healthcare stocks delivered over 1,000% total returns compared to 1% of non-healthcare stock.

> **While diversification is always important, it is arguably even more important when investing in Healthcare given the wide range of possible outcomes.**

Distribution of total returns over 10-years



Source: TD Asset Management Inc., as of Dec 31, 2022.

While diversification is always important, it is arguably even more important when investing in Healthcare given the wide range of possible outcomes. Investors in the sector should seek to not only diversify between different securities, but also diversify across the different industry segments which include pharmaceuticals, biotech, medical devices, life science tools, health information technology and managed care.

An ETF with broad healthcare exposure

At TD Asset Management Inc., we are committed to providing one of the broadest offerings of investment solutions in Canada and the essential building blocks needed to help you construct a well-thought-out portfolio.

The primary goal of TDOC is to provide investors with broad based global exposure to Healthcare, in order to capitalize on the secular trends driving growth in the sector — without the risk of investing in a narrow niche or industry group.

TDOC provides exposure to nearly 140 mid, large and mega-cap names, capturing both mature industry leaders and healthcare innovators. This includes Pharmaceuticals, Biotechnology, Life Science Tools, Healthcare Equipment, Healthcare Services, and Health Technology.

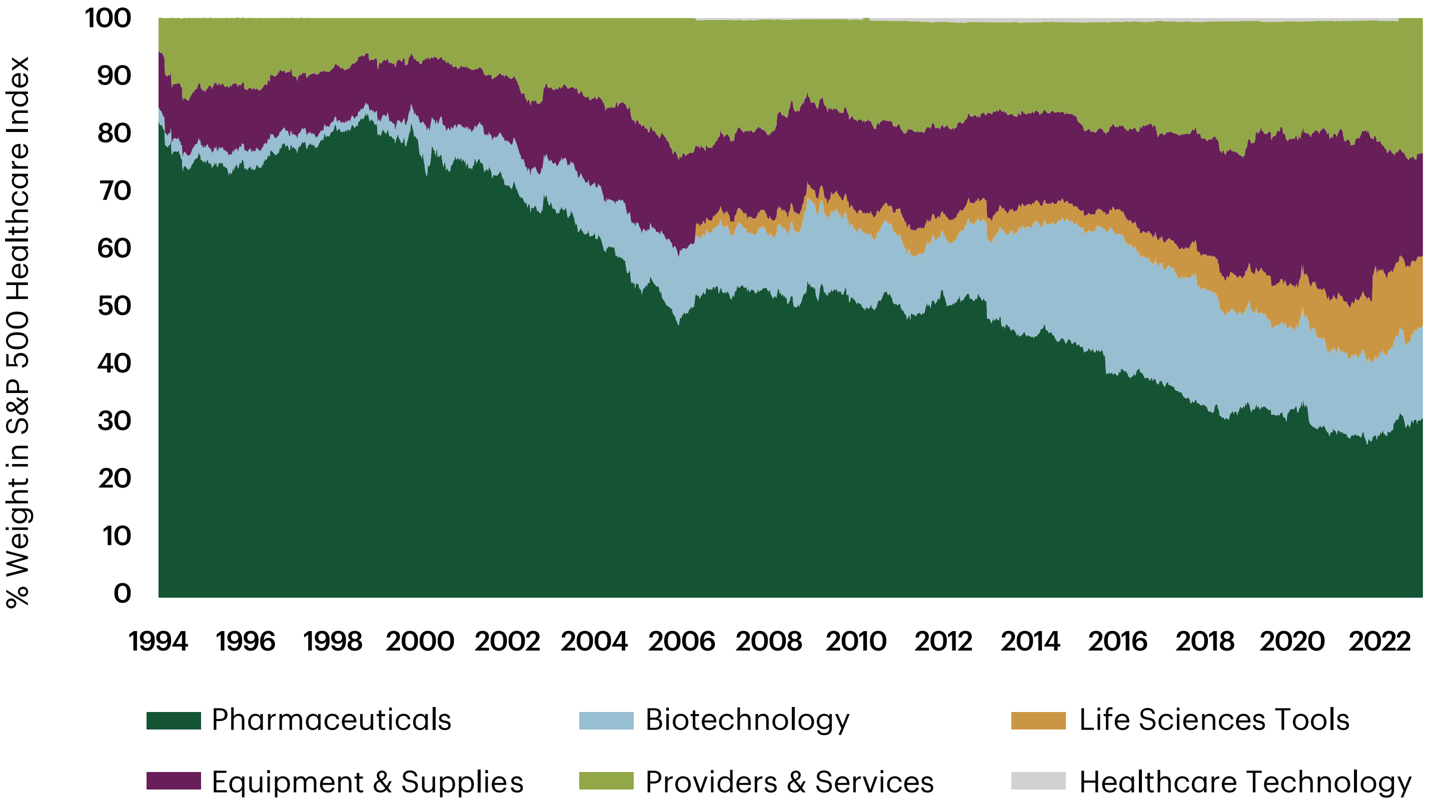
What separates TDOC from the rest?

Not all ETFs are created equal and there are four primary types of healthcare ETF products on the market today: niche, covered call, market cap weighted and equal weight approach. The table below highlights some key differentiators between TDOC and the others.

ETF Type	Broad Healthcare Exposure	Reduced Exposure to Mega-Cap Pharma	Global Exposure	Management Fee
Market Cap Weighted ETFs	✓	✗	✓	Competing ETFs range from 0.35% to 0.63%
Equal Weight ETFs	✓	✓	✗	
Niche Healthcare ETFs	✗	✗	✗	Competing ETFs range from 0.45% to 0.85%
Covered Call ETFs	✗	✗	✗	
TD Global Healthcare Leaders Index ETF (Solactive Global Healthcare Leaders Index)	✓	✓	✓	Attractively priced at 0.35%

One feature of TDOC is that it caps the weight of individual securities at 2% and excess weight is redistributed to other index components on a pro-rata basis at each rebalancing interval. This tilts exposure away from slower growing mega-cap pharmaceutical companies to faster growing biotechnology, health equipment, and life science tools companies. As illustrated in the chart below, we've seen other areas of healthcare outperform mega-cap pharmaceuticals over the past two decades — a trend we expect will continue.

S&P 500 Healthcare Index - Industry Compostion



Source: TD Asset Management Inc., as of Dec 31, 2022.

TDOC is designed to help meet the evolving needs of investors and includes strategies that we believe are truly distinctive in the marketplace. TD ETFs provide more choice and opportunity for investors in the fast growing Canadian ETF market.

Strategy

For more information about TDOC, or TD ETFs in general, please visit TD.com/ETFs

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