

Views from the Desk

Updates in the Equity and Fixed Income Market

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Rate Announcements and Bond Market

The Fed followed through with their 75bps rate hike (that was expected due to high CPI print). The Fed had direct and forceful language explaining that they are strongly committed to return inflation back to the 2% objective. We should see another 75bps rate hike in July from the Fed which hopefully will have meaningful impact on tapering inflation. The BoC may follow suit with a 75bps rate hike as well. The inflation print in Canada came in at 7.7% this morning. Inflation is the number 1 goal for central banks, and we shouldn't be surprised if the central banks overshoot with rate increases, and if overshoot, could potentially cause a recession. We think there is upward pressure on the yield curve as it flattens out and we believe short corporate bonds to be the better trade for fixed income. [ZST - BMO Ultra Short-Term Bond ETF](#), [ZCS - BMO Short Corporate Bond Index ETF](#), [ZCDB - BMO Corporate Discount Bond ETF](#)

Spreads

Corporate bonds have been hit hard YTD and we are seeing a buying opportunity for corporate bonds. Corporate spreads haven't been at these current levels since 2013 and we are about 30 to 35bps wider than what we've seen in the last 10 years. We think the widening of spreads YTD has a lot to do with bonds being oversold. High yield bonds have widened more relative to investment grade (IG). We do see IG being more prudent in a portfolio (leaning toward a recession). Investors should consider adding corporate exposure to take advantage of spread tightening. [ZSU - BMO Short-Term US IG Corporate Bond Hedged to CAD Index ETF](#), [ZUS.U - BMO Ultra Short-Term US Bond ETF \(USD Units\)](#), [ZCDB - BMO Corporate Discount Bond ETF](#) and [ZQB - BMO High Quality Corporate Bond Index ETF](#)

Dividend ETF strategies

We think the dividend factor will continue to do well going forward. Staying invested during these times of uncertainty is very important to avoid being wrong with trying to time the market. Dividend equities tend to have less risk than broad beta equities. The rising risk of inflation tends to favour dividend blue chip companies. The last 3 months returns have outperformed the broad market by approximately 3% to 4% in the US and Canada. [ZDY - BMO US Dividend ETF](#), [ZDV - BMO Canadian Dividend ETF](#)

Covered Calls

Elevated volatility can be beneficial to generate additional income to your portfolio. The VIX tends to be a mean reverting asset class. The long-term average for the VIX is 15. When the VIX is below 15 it tends to drift back up and when it's above 15 it tends to drift back down. COVID was a dramatic event that sent the VIX to all time highs of about 80 and it has since come back down however, it has stayed around 20 to 30. The VIX trend seems to be staying at these new heightened levels and at these levels our covered call strategies have been able to general above average premiums. BMO writes on half of our covered call portfolios and tend to write further out of the money when volatility is up and closer to the money when volatility is low [ZWC - BMO Canadian High Dividend Covered Call ETF](#), [ZWH - BMO US High Dividend Covered Call ETF](#), [ZWG - BMO Global High Dividend Covered Call ETF](#), [ZWP - BMO Europe High Dividend Covered Call ETF](#).

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Utilities

[ZUT - BMO Equal Weight Utilities Index ETF](#) and [ZWU - BMO Covered Call Utilities ETF](#) are performing well this year. There is a preference towards lower risk solutions and utilities specifically has been an interesting satellite position for defensive equities. Utilities are not only a great yield generating investment, but they also can have inflation hedge characteristics as some of their revenues are tied to cost and inflation. Utilities is a defensive sector with less risk which is leading to outperformance in this late business cycle. ZWU specifically has a distribution yield of approx. 8% and carries Energy Pipelines and Telecoms to round out the portfolio.

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Source: Bloomberg, All returns and data points June, 2022.

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