Views from the Desk

Updates in the Equity and Fixed Income Market

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Inflation

There are a lot of headwinds in Europe with the energy crisis standing out (concerns of energy supply and costs throughout the winter). Some European governments are talking about shutting down manufacturing plants to save energy. If so, they could be hurting GDP growth and cause significant damage to the economy. Currencies are dropping and the BoE is propping up the British Pound (which is at multi decade lows). We think there could be a recession coming soon for Europe. We recommend a flight to quality companies within Europe. ZEQ - BMO MSCI Europe High Quality Hedged to CAD Index ETF

With the strong USD we will see U.S multi nationals slow down. The BoC appears to be ahead of inflation compared to other major developed countries due to large rate hikes at the beginning of the year. We think Canada may outperform for the rest of 2022. Overweight Canada, neutral U.S and underweight Europe is how we look to position ourselves for the rest of 2022. ZCN - BMO S&P/TSX Capped Composite Index ETF, ZSP - BMO S&P 500 Index ETF, ZEQ - BMO MSCI Europe High Quality Hedged to CAD Index ETF

Fixed Income Expectations

Forecasts are starting to show we are nearing a peak in 10-year rates. U.S 5- and 10-year rates spiked, however, we may see more rate volatility going forward as the market is digesting economic news very quickly. ZAG - BMO Aggregate Bond Index ETF has had a challenging year and peak rates will lead to upside in the aggregate. As we are nearing the "hopeful peak" of 10-year rates ZAG is very well positioned across the yield curve and doesn't require you to necessarily time the market. We still look to compliment your aggregate bond portfolio with short term bonds in favour of credit. ZST - BMO Ultra Short-Term Bond ETF, ZCS - BMO Short Corporate Bond Index ETF, ZQB - BMO High Quality Corporate Bond Index ETF, ZCDB - BMO Corporate Discount Bond ETF are great options available.

Dividend Factor

ZDV - BMO Canadian Dividend ETF is outperforming the TSX by approximately 6% year to date. ZDV doesn't have any exposure to the technology sector and is overweight in the staples and telecoms sectors which are more defensive. ZDY has varying exposure across many sectors and has outperformed the S&P 500 by approximately 9%. The names within the dividend ETFs have contributed to performance as there is a tilt to cash generative companies (cash is king in an inflationary environment).

Cash Alternative ETFs

It is common to see cash alternative ETFs gather assets in risk off environments as investors wait for volatility to subside. We have seen 300 million flow into ZST - BMO Ultra Short-Term Bond ETF and 125 million into ZUS.U - BMO Ultra Short-Term US Bond ETF (USD Units) recently. Looking at ZST and ZUS.U we see an advantage over other cash like products since it offers an attractive yield, better protection during a rising rate environment, high liquidity, and no lockup period. These two ETFs purchase bonds that mature in 1 year or less and hold to maturity. The yield will naturally increase in a rising rate environment since low-cost bonds with higher yields are moved into the portfolio as high-cost lower yield bonds mature. Investing Cash in Ultra-Short Term Bond ETFs

Preferred Shares

ZPR - BMO Laddered Preferred Share Index ETF There was a selloff in prefs since there was a negative widening in credit spreads. There are strong tailwinds within the portfolio as banks issue LRCNs and redeem prefs... for more on this topic please listen to the BMO Podcast.

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

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