Views from the Desk

Updates in the Equity and Fixed Income Market

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Fixed Income

We were seeing some moderation in inflation, giving investors some hope that the rate cycle was coming to an end. However over the past few months there has been a bit of a reversal. CPI came in a little hotter than expected in Canada yesterday at 0.6% for one month and 3.3% for the one year. Both in Canada and the US the 10 Year yields are at 15 year highs. This could be an opportunity to add some duration to the portfolio that can balance out against equities and also provide a strong level of yield. We gave no shortage of very precise fixed income tools in terms of ETF exposures. To highlight one that could potentially work very well is **BMO Corporate Bond Index ETF (Ticker: ZCB)**. It is the universe of Canadian investment grade corporate bonds, BBB and above, duration just under 6 years and a YTM of about 5.67%. So with yields this high, it can be an opportunity to add duration and increase yield to the overall portfolio.

Low Volatility

The low volatility factor has lagged versus the broad market on the YTD basis. We've seen a strong growth rally mainly driven by tech companies this year. Low vol strategies tend to lag during these type of market rallies because they hold less risky stocks, to accomplish less draw downs during market downturns. To win by not losing. Given there is still lot of headwinds in the equity market driven by monetary policy and inflation concerns, we are still constructive on the low vol factor as it can help balance that risk. Paring **BMO Low Volatility US Equity ETF (Ticker: ZLU)** with a growth factor ETF like **BMO NASDAQ 100 Equity Index ETF (Ticker: ZNQ),** can help create a barbell approach to provide a better risk adjusted risk versus the broad market.

Canadian Bank Earnings

Earnings are right around the corner, and expectations are a bit of weakness with cash earnings down about 5%. The market is recognizing the risk with higher interest rates, putting pressure on loan books and the banks putting aside credit provisions. It is often a good time to buy banks when they are building those credit provisions. Right now Canadian banks are trading at a 9.5x forward P/E, an attractive level versus historical averages. The average dividend yield is about 5.2% right now. Investors can get exposure through **BMO Equal Weight Banks Index ETF (Ticker: ZEB)**

U.S Banks

Fitch Ratings Agency warned of a possible downgrade to US Banks, this is only a few months after we had significant volatility related to the regional banking crisis. So there is some sensitivity around US banks. They just went through an earnings season with strong results and fundamentals. We are cognizant of a hard landing, but we are still seeing that soft landing scenario. Overall, we think there's an opportunity with US banks, a satellite in terms of portfolio positioning. **BMO Covered Call US Banks ETF (Ticker: ZWK)** can be a good way to get exposure to help covert the price volatility into income and get US dollar exposure should we have an economic slowdown.

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Oil & Gas

During the summer we've seen a record level of demand for oil, due to summer air travel, power generation and fueling the Chinese economy, especially in the petrochemical activities. Most importantly, OPEC cuts to maintain pricing power has also driven up prices. Another source of potential future demand is the US Strategic Petroleum Reserve (SPR). The SPR has been depleted last year due to supply constraints, so they will need to stockpile the reserve. For investors looking for exposure, **BMO Equal Weight Oil & Gas Index ETF (Ticker: ZEO)** holds an equal weight of blue chip energy companies. For more conservative investors who want more of an income tilt, they can look to **BMO Covered Call Energy ETF (Ticker: ZWEN)**.

Source: Bloomberg, All returns and data points July 2023.