

Views from the Desk

Updates in the Equity and Fixed Income Market



Alfred Lee & Chris McHaney, BMO ETFs

Asset Allocation

Correlation does not equal causation and obviously the Superbowl doesn't control the stock market. The Superbowl is a fun indicator that started back in 1973, accurate about 73% of the time, but it was wrong in the past 6 of 7 years. So, there is no secret sauce to investing or crystal ball. Long term investing takes discipline, understanding your investment objectives. Setting the right plan, sticking to your asset mix, regular review, and making changes around the edges. Asset allocation ETFs can help achieve this. **ZBAL – BMO Balanced ETF** and **ZGRO – BMO Growth ETF** are two great options. Holding different ETFs can help create risk differentiated portfolios, between asset mixes, to help investors stay true to their objective for the long run. Holding asset allocation ETFs as core and adding ideas that we discuss on this podcast as satellites. The Superbowl indicator is a fun one, it always comes up in January, but again it is all about sticking to your strategic asset allocation and staying disciplined.

US CPI

Markets were all over the board after the release of the US CPI print. Digging deeper into the numbers, inflation is trending down on the goods side and we expect that to continue. Inflation proved to be more resilient on the services side. Core inflation ex housing and energy, fell back to October levels. A couple short term risks that can skew inflation higher – China reopening and strategic petroleum reserves. Markets are gauging the likelihood of rate cuts this year. The overnight interest rate swap market is pricing in a cut, which maybe unlikely, we think we are very close to the terminal value, which is good for the bond market. **ZUAG – BMO US Aggregate Bond Index ETF** is a great way to gain exposure to a well diversified US bond market. Benefiting from exposure to US credit, short and long duration, it is a solid building block in a portfolio. From a tactical perspective, with spreads tightening in IG bonds, inversion of yield curve, duration and credit exposure can come in handy. ZUAG's current YTM: 4.3% and Duration: 6.3. From a Canadian investor's perspective, if you own Canadian bonds and equities, your owning the same companies across the capital structure. Getting US bond exposure gives you that corporate diversification.

Buybacks and Taxes

Democrats passed a 1% tax on buybacks that begins this year. Corporate announcements in January of significant buybacks signals the 1% tax isn't causing companies to rethink their buyback programs. \$132 Billion in buybacks in total were announced, triple from last year. Energy companies were leading the charge; Chevron and Exxon. Meta as well with a \$40B buyback. Biden favours increasing the tax to 4% or more, we don't see that happening in the near term with Republicans controlling the house. If taxes were to increase this could cause more dividends to be paid out. For US dividend ETFs, what we like to focus on is free cash flow generation for dividend payments. BMO Dividend ETF's identify companies with strong operating cash flow, selecting healthy companies that can increase their dividend. **ZDY – BMO US Dividend ETF** for example is not just screening for high dividend payers, but sustainable growers using cash flow from operations. So, for non Canadian dividend ETFs, our dividend methodologies can lead to strong outcomes with the businesses you are invested in.

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Buy American Act

This Act has been around since 1933. But the major difference is there is real bipartisan support. And with the increasing trend of deglobalization, this policy has more legs. It applies to all US government agencies when making purchases over \$10,000 for public use, the goods must be made in the US. This is supportive of US equities. Obviously other factors will drive equity performance, but this is a tailwind. We believe this can benefit US mid and small cap companies. Inside **ZSML - BMO S&P US Small Cap Index ETF** you will find names like Olympic Steel and Kaiser Aluminum. In **ZMID -BMO S&P US Mid Cap Index ETF** - US Steel and Cleveland Cliffs, these names could benefit from the Buy American Act and are not typically on investors' radars. Getting that exposure through an ETF, a broad basket of securities, can largely benefit from this policy initiative. Sectors that may benefit are industrial, materials, & information technology. These sectors make up 35-45% on average in ZMID and ZSML.



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

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