Views from the Desk

Updates in the Equity and Fixed Income Market

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Silicon Valley Bank

It was a pretty eventful weekend starting on Friday with Silicon Valley Bank ending in receivership along with Signature Bank. With low rates during the pandemic, customers of Silicon Valley Bank became flush with cash and so their deposits increased significantly. Since demand for loans were relatively low, SVB took on more duration risk with deposits to widen their spread. With rates rising as fast as they did, those bonds sold off quite a bit and that portfolio became worth less than the value of their common equity. They tried to issue more equity to shore up capital, but depositors in fear started a run on the bank, sending the stock price into a free fall, until it failed to open. The fear spread to other regional banks and Signature Bank as well. Now, the Fed has a bit more breathing room to take their foot off the gas. After these events, a 25 bps increase is more likely. CPI came in at 6%, the previous reading was 6.4%, so it is trending in the right direction.

Financials

The collapse of Silicon Valley Bank and Signature Bank caused a lot of volatility in the financial sector. First Republic and Western Alliance were both halted due to the volatility, this has impacted **BMO Equal Weight US Banks Index ETF (Ticker:ZBK)** with wider spreads. So, we advise to use limit prices when trading. Also reach out to your ETF Specialist as well to help guide you through best execution. Also, due to the increased volatility we were able to monetize more option premium in **BMO US Covered Call US Banks ETF (Ticker:ZWK),** we rolled down some our call options to take advantage. The SVB and Signature collapse should not have major negative implications for Canadian banks. The Canadian banking system is one of the best in the world and they have diversified business lines across industries. There are some sore spots, small impacts on US acquisitions made by BMO and TD, are possible. BMO acquired Bank of the West and TD purchased First Horizons. These could have small implications for growth within the banks. But not a major concern, Canadian banks have a record of consistent and resilient performance through many economic cycles.

Bond Market Volatility

Interest rate volatility hasn't been this high since 2009. Just a week ago the market was pricing in a chance of a 75 to 100 bps increase. The likelihood is that we may be getting a 25 bps at most. With ETFs and BMO's fixed income ETF matrix, allows investors to quickly reposition their fixed income portfolios given changing market conditions, not just with duration, but credit as well. So everything from short corporate ETFs to long Federal; **BMO Short Corporate Bond Index ETF (Ticker:ZCS)** and **BMO Long Ferderal Bond Index ETF (Ticker:ZFL)**. 10 to 15 years ago, investors would have had to do this through single bonds, which are a lot more difficult to execute.

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Equities

The good news is that if this contained to the US banking sector, it is not spreading to the larger names like JP Morgan, and if the Fed and regulators have done enough, this can prevent the contagion. The silver lining is that this may cause the Fed to pause on interest rates sooner than previously expected, which is good for risk assets in general. So, if investors are longer term bullish, they can use an ETF to take advantage of the recent sell off. There are lot of options, including looking at the Canadian banks that are very well capitalized and trading at attractive valuations, with **BMO Equal Weight Canadian Banks ETF (Ticker: ZEB)**. For those seeking more income, **BMO Covered Call Canadian Banks ETF (Ticker: ZWB)**. For investors looking for even more broad exposure, **BMO S&P 500 Index ETF (Ticker: ZSP)**, **BMO NASDAQ 100 Equity Index ETF (Ticker: ZNQ)**, or **BMO Dow Jones Industrial Average Hedged to CAD Index ETF (Ticker: ZDJ)** provide easy access to broad equities if you believe this will be contained to just the US banking sector.

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