Views from the Desk

Updates in the Equity and Fixed Income Market

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Investing with Cautious Optimism- Equities

The reports of new virus cases are lowering, improvements for therapies for Covid-19 are being reported and historical amounts of fiscal and monetary stimulus are flooding the market. This has all been positive for equities and we have seen this has the S&P 500 has rallied 21% since the end of March. However, the coming realization that the recovery will be prolonged and remains a headwind. There will also be a lot of bad economic data coming out that the market will have to navigate in the coming weeks and months. The outlook for volatility in the near-term is still elevated. Overall, we are cautiously optimistic for equities for the next 12 months. In this environment we highly advocate for Low Volatility and Quality equities. Low Volatility's sector exposure is defensive with an overweight to Utilities and Consumer Discretionary, sectors which will do well in this new work from home, stay home, environment. As a compliment to Low Volatility, we also really like Quality. In the US, Quality is up on the year (+1%). These are companies with low debt and strong balance sheets. It also has an overweight to large cap Tech names, so we think this pairs nicely with the defensive sectors within Low Vol.

Investing with Cautious Optimism- Fixed Income

We think investors should trade up in quality in their fixed income exposures as a general theme. We see the corporate space as attractive; with interest rates as low as they are, credit will offer a yield-pickup to government bonds. Within the corporate space, the highest quality companies are most attractive right now. **BMO's High Quality Corporate Bond Index ETF (ZQB)** is an ETF with corporate bonds with an A and above rating. This means that if these bonds get downgraded, they remain investment grade. If you want to add a little more risk, and boost your yield, look to the BBB sector. It works as a satellite position or, keeping with the theme of upgrading quality, replacing your High Yield bonds with BBBs. BMO's **BBB Corporate Bond Index ETF (ZBBB)** offers an ETF with a portfolio of BBB rated bonds. These are still IG bonds but they offer a higher spread vs government bonds. In terms of Energy exposure, ZQB has a very low energy weight, (sub 5%) while ZBBB is around 32% of the portfolio.

Covered Call Strategy Update

The high level of market volatility has been positive for the covered call option strategies. Right now we are writing options around 10%-15% out-of-the-money which is adding 2-4% more incremental income to each fund. We really like the **BMO Global High Dividend Covered Call ETF (ZWG).** It is a one-ticket global covered call solution with exposures in US (60%) Canada (10%), Europe and Asia. This is also a mega-cap strategy: it holds the largest global companies which pay sustainable dividends. Since the ETF launched in mid-Jan, the MSCI World Index is down 10% and this fund is down 8% so it has added 2% of value for investors during this time. The yield is about 7% so this makes a great defensive growth solution for today's market environment.

Investing in the Energy Sector

With futures-based ETFs, we say "buyer beware". Given market volatility in futures markets I would stay away from these types of products. Many investors might not realize that by holding these contracts, they are holding actual barrels of oil, and anyone holding the contract at expiry means they must take delivery of the oil. In May there was a massive oversupply to the point where the contract went negative. The price of the June contract is $14 right now, half the value of long-term oil prices. Some futures ETFs still have exposure to the June contract so investors should be very careful. We think a better approach to exposure to Energy right now is through Canadian Energy equities, especially the senior names. **The BMO Equal Weight Oil & Gas Index ETF (ZEO)** holds 9 large-cap Energy names, all of which are in the TSX 60. Half of these holdings are pipelines which are less economically sensitive to the price of oil.

HISA ETFs These ultra-short term, cash like investments have seen a huge amount of inflow in the last couple years. But in the last few months these flows have really slowed down. Because yield has come down quite a bit, especially on the short end, these products do not offer the yield-pickup vs Savings Accounts they once did. But their main benefit right now is liquidity. When investors begin to put their money back into the market, they will be able to access their cash very easily with a product like this.

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