

THIS WEEK WITH SADIQ



February 21 to 25, 2022

Political Headlines, Treasuries, Earnings

Weekly Commentary

Political Headlines

COVID has dominated headlines for nearly two years, but now, with the situation improving, political issues have re-emerged. In Europe, there's tension brewing over the Ukraine-Russia confrontation; in the United States, midterm elections are on the horizon; and in Canada, there's the federal government's invocation of the Emergencies Act in response to ongoing protests and blockades. But what impact could these developing issues have on the equity market? On their own, any of these stories would be worrying, but with the prevalent risk-off sentiment they become a major concern. Markets were already having trouble generating momentum because of existing issues like rising interest rates, high inflation, and supply chain bottlenecks. It's unlikely that all these headwinds will be resolved simultaneously, which means that volatility will likely remain high for the rest of 2022.

Bottom Line: Equity prices may continue to rise, but investors should expect bumps in the road.

Treasuries

Over the last two weeks, we've seen the 10 Year U.S. Treasury Yield cross the 2% mark. From an equity market perspective, we don't think there's reason to be concerned, but it is something of a mental barrier for investors. Does it signal a liquidity crisis? We don't believe so. Back in March 2020, liquidity was a major issue as markets went downhill, and the Fed had to step in to provide support. The situation now is very different. Investors are seeking safe haven assets to manage their equity risk, and as yields rise, treasuries become that much more attractive. This is especially true in Canada and the U.S., given that in other parts of the world we continue to see negative yields.

Bottom line: If yields hit 2.5% or 3%, that's when the debate over bonds versus equities will really begin.

Earnings

More companies have announced corporate earnings over the past couple of weeks, and in general, the numbers are exceeding analysts' expectations. But it's important to make a distinction between official estimates and what you might call "whisper" estimates—numbers that are tacitly expected but not publicly announced. In the case of some larger companies, including big names in tech like Meta (formerly Facebook) and Nvidia, those whisper estimates aren't being met and stock prices are taking a hit as a result. What we're seeing is a resetting of where earnings and valuations should be after two years of anticipation-fueled growth. Our view is that markets have been level-setting not only for the last month, but for the last six months or more.

Bottom line: Once a new equilibrium is set, we may see markets lift off again.

Positioning

Recently, we've been heavy on sectors tied to reopening, and we still think that's the right strategy for the short term. Airlines and Financial continue to do well, and while Energy has recently come off somewhat because of the Ukraine-Russian tensions easing slightly, we anticipated that and reduced our exposure as a result. Now, we're starting to look at our positioning over a somewhat longer term—what might be an attractive play in the next two

Expert

Sadiq S. Adatia

Chief Investment Officer BMO
Asset Management

Mr. Adatia joins BMO AM from Sun Life Global Investments, where he most recently held the role of Chief Investment Officer. Prior to that, he held investment roles at Russell Investments Canada and Mercer Canada. He holds an Honours Bachelor of Mathematics degree in Actuarial Science & Statistics from the University of Waterloo. He is also a CFA Charterholder and is a Fellow, both of the Society of Actuaries (Investment Specialty Track) and the Canadian Institute of Actuaries.



to three years? For instance, some of the technology companies that have taken a beating recently may be prime candidates over a two-to-three-year period. Though we haven't made any positional changes yet, we think it's wise to consider categories that may take a little more time to prosper but that have strong upside over a longer time frame.

Bottom line: While markets are available at a discount, we see opportunities to add greater equity allocation to the portfolio.

As Chief Investment Officer, Sadiq S. Adatia's views directly influence the [BMO ETF Portfolios](#).

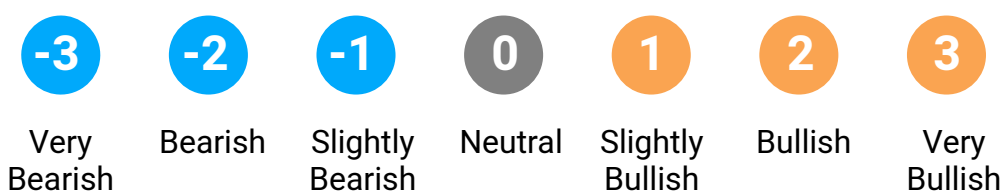
Market Update

- Equity markets posted another choppy week with more inflationary North American data pointing to rate hikes, as well as ongoing will-they-or-won't-they fears of a Russian invasion of Ukraine
- The S&P 500 closed the week down 1.6% with consumer staples posting the only gain among sectors. Meantime, the TSX dropped 2.5% as one of the worst performers of the week, though it remained firmly above its 200-day moving average
- A flatter yield curve sparked fears of a recession; while the 10s/2s spread has narrowed this month, we'd note that at around 50 bps, it's currently off Monday's lows. Gold rallied this week, though it has stepped back from earlier highs, and oil ended a volatile week up 2% to around \$91.70.

Asset class views, as of February 2022

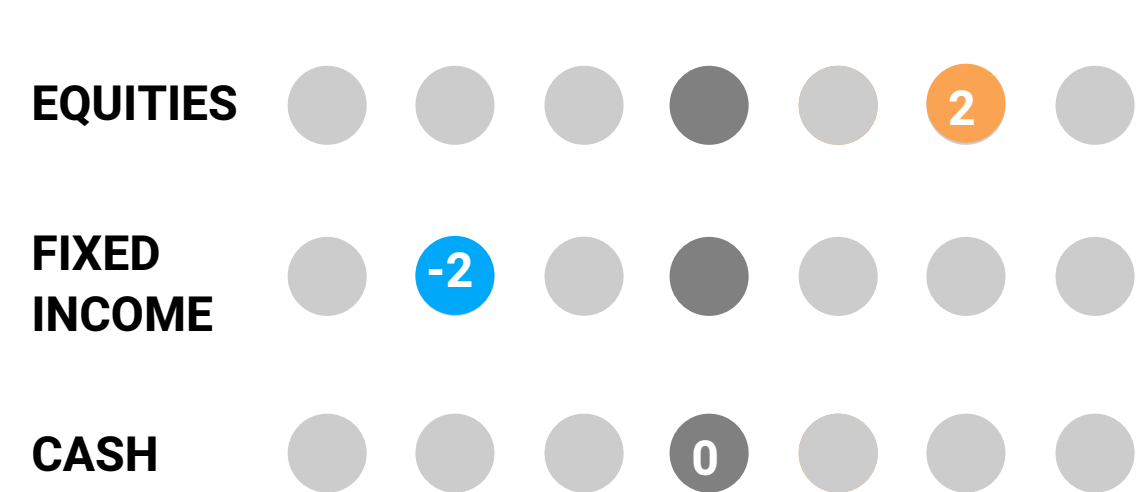
Monthly Perspectives

At BMO Global Asset Management, we recognize that asset allocation is the primary driver of long-term portfolio performance. That's why our Multi-Asset Solutions Team (MAST) has developed a simplified "Five Lenses" view to help explain what is driving their asset allocation decisions.



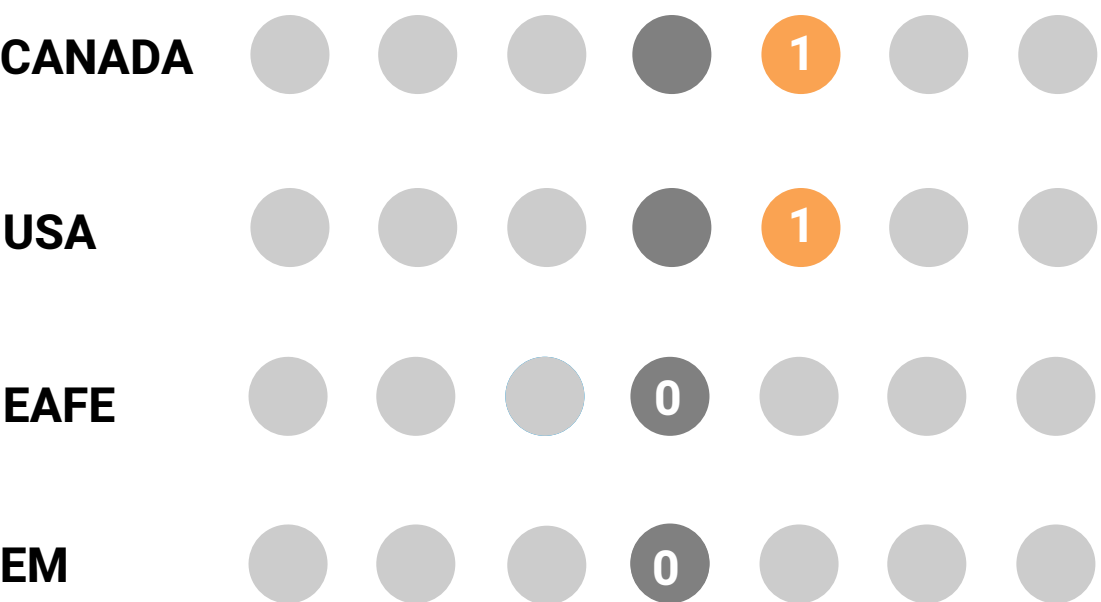
Asset Mix

- COVID-19 and Omicron are lingering but no longer posing a material threat to the economic outlook, especially in the U.S.
- We expect global growth to cool but to remain above trend in 2022 while inflation remains elevated.
- Strong earnings growth should more than offset equityvaluation headwinds from rising rates in 2022.



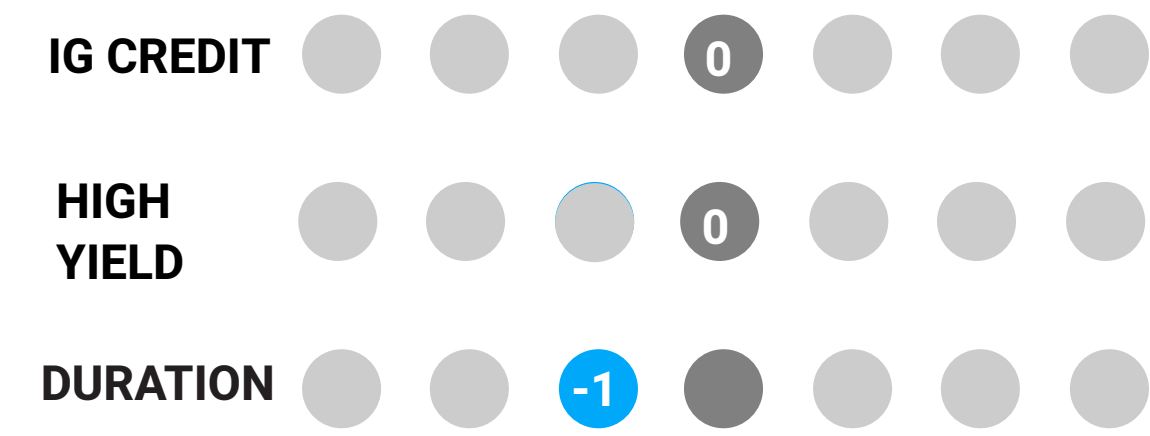
Equity

- North America continues to offer the best risk-reward outlook, especially after the weak year-to-date performance of U.S. equities. Mid-cycle dynamics and energy-driven inflationary pressure favour the U.S. and Canada.
- Although China's economic outlook remains soft, market negativity on EM and EAFE equities has probably peaked.



Fixed Income

- March is widely expected to see the U.S. Federal Reserve (the “Fed”) and BoC start normalizing interest rates, probably at a fast pace throughout 2022.
- Government bonds and bond duration remain unattractive as central banks are about to hike while the growth and inflation outlook remain strong.



Style/factor

- Mid-cycle dynamics along with anxiety over Fed hikes favours higher quality stocks, whose revenues and earnings are more predictable and less sensitive to swings in economic expectations



Implementation

- Bank of Canada may hike interest rates sooner than other central banks which would support the currency, versus heavy commodity-importing currencies such as the Euro and Japanese Yen.

Thank you for reading!

Disclosures:

The viewpoints expressed by the Portfolio Manager represents their assessment of the markets at the time of publication. Those views are subject to change without notice at any time without any kind of notice. The information provided herein does not constitute a solicitation of an offer to buy, or an offer to sell securities nor should the information be relied upon as investment advice. Past performance is no guarantee of future results. This communication is intended for informational purposes only.

BMO Global Asset Management is a brand name that comprises BMO Asset Management Inc., and BMO Investments Inc.

Any statement that necessarily depends on future events may be a forward-looking statement. Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions. Although such statements are based on assumptions that are believed to be reasonable, there can be no assurance that actual results will not differ materially from expectations. Investors are cautioned not to rely unduly on any forward-looking statements. In connection with any forward-looking statements, investors should carefully consider the areas of risk described in the most recent simplified prospectus.

This article is for information purposes. The information contained herein is not, and should not be construed as, investment, tax or legal advice to any party. Investments should be evaluated relative to the individual’s investment objectives and professional advice should be obtained with respect to any circumstance.

Commissions, management fees and expenses (if applicable) all may be associated with investments in mutual funds. Trailing commissions may be associated with investments in certain series of securities of mutual funds. Please read the fund facts, ETF facts or prospectus of the relevant mutual fund before investing. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated. Distributions are not guaranteed and are subject to change and/or elimination.

For a summary of the risks of an investment in the BMO Mutual Funds, please see the specific risks set out in the prospectus. ETF Series of the BMO Mutual Funds trade like stocks, fluctuate in market value and may trade at a discount to their net asset value, which may increase the risk of loss. Distributions are not guaranteed and are subject to change and/or elimination.

BMO Mutual Funds are managed by BMO Investments Inc., which is an investment fund manager and a separate legal entity from Bank of Montreal.

®/TM Registered trade-marks/trade-mark of Bank of Montreal, used under licence.