June 29, 2023

US Strategy Snapshot

2023 Mid-Year Outlook

Bottom Line: Needless to say, 1H market performance has been quite impressive (~14%), and we would expect the momentum to persist during 2H, albeit at a slower pace judging by our 4,550 year-end S&P 500 price target. From our perspective, all the worries that damaged 2022 market performance are slowly beginning to subside (inflation/Fed). Yes, earnings growth is likely to remain a sticking point, but we believe investors fully understand this and are looking past 2023 results and expecting growth to reaccelerate in 2024 and beyond. In addition, we believe seasonality provides another tailwind as the S&P 500 has never posted a 2H loss following such a strong 1H, post WWII. The bogeyman of narrow market breadth has started to broaden out and is a trend we expect will continue. Selectivity will be key, as will owning a "little bit of everything," but we are still tilted toward value and SMID-cap in our size and style preferences.

Main Points:

- The Path to Our S&P 500 2023 Year-End Price Target
  - ✓ Further gains are likely, but pace should slow alongside a bumpy path
- Strong Price Returns During First Half of Calendar Year Typically Lead to Further Market Gains in Second Half
  - ✓ S&P 500 gains an average of 11% during 2H when 1H gains range between 10%-15%
- Corporate Earnings Remain Resilient
  - ✓ 2Q23 is likely to represent the EPS growth trough with a strong acceleration expected in 2H
- Sector Review and Outlook
  - ✓ Communication Services and Technology remain top picks with Financials as our contrarian value play
- Lean Toward Value, but Also Incorporate Growth
  - ✓ Value appears extremely oversold while growth is expensive vs. its earnings outlook
- SMID-Caps Showing Signs of Life With Relative Valuations Versus Large Caps Still Near 20-Year Lows
  - ✓ Steep relative valuation discounts and improved revision trends should benefit SMID

Implementation Strategies:

- US Tactical Equity and US Disciplined Value portfolios
- Please see US Strategy Portfolios and Investment Strategy Portfolios for recent changes

For disclosure statements, including the Analyst Certification, please refer to page(s) 9 to 12.

BMO Capital Markets

Investment Strategy

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US Strategy – S&P 500 Targets

Price Target Model	2023E
DDM	4,750
Fair Value P/E	4,350
Price Target	**4,550**
EPS Target Model	**2023E**
Macro Regression	$215
Bottom-Up Consensus	$220
Normalized EPS	$200
EPS Target	**$220**
Implied P/E	**20.7x**

Source: BMO Capital Markets Investment Strategy

US Strategy – Recommended S&P 500 Sector Weightings

Sector	Opinion	Tgt. Wgt.
Communication Services	OW	9.5%
Consumer Discretionary	MW	10.25%
Consumer Staples	UW	5%
Energy	MW	4%
Financials	OW	13.5%
Health Care	MW	13.75%
Industrials	MW	8.5%
Information Technology	OW	29%
Materials	MW	2.5%
Real Estate	MW	2.5%
Utilities	UW	1.5%

Source: BMO Capital Markets Investment Strategy

OW: Overweight
MW: Market Weight
UW: Underweight

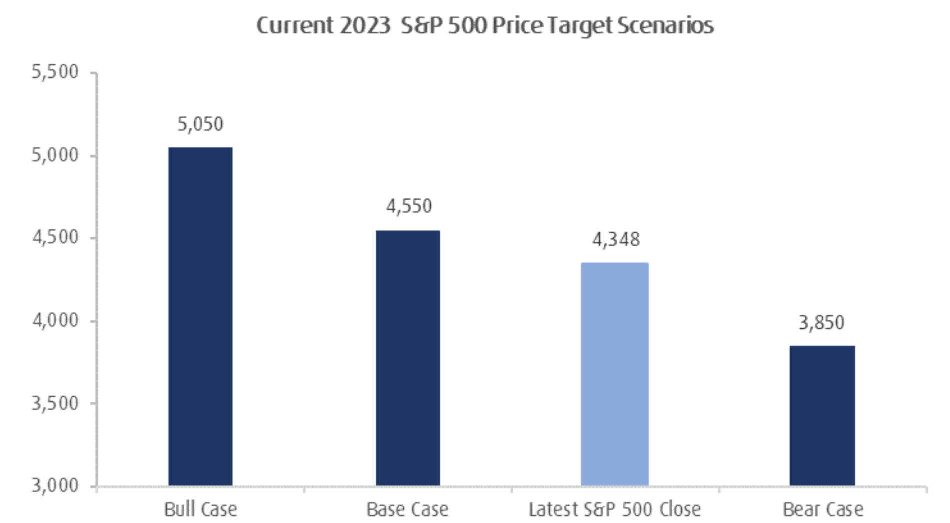
13:59 ET~

The Path to Our S&P 500 2023 Year-End Price Target

Our S&P 500 Year-End Price Target of 4,550 Implies Additional Upside in 2H of the Year

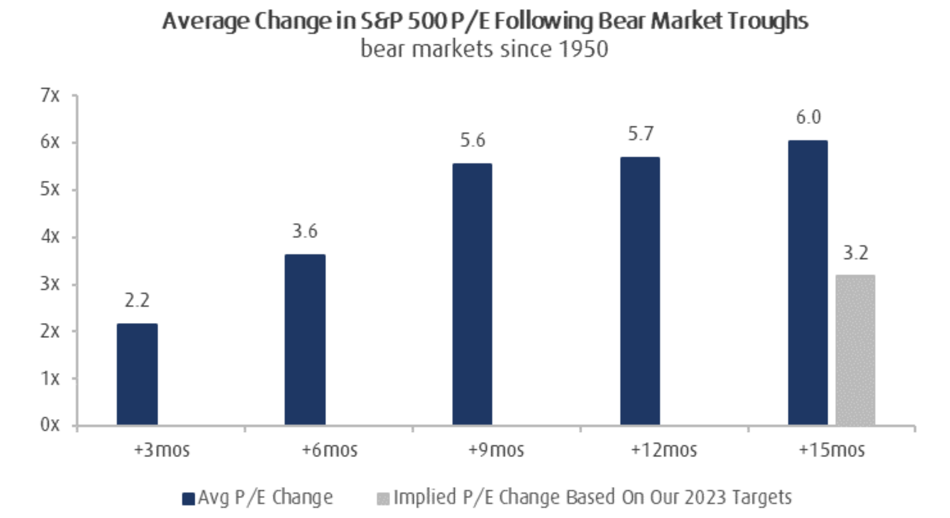
Source: BMO Investment Strategy Group, FactSet.

Base Case Calls For ~5% Gain From Latest Close, While Bull Case Points to New SPX High



Source: BMO Investment Strategy Group, FactSet.

Multiple Expansion Should Drive Further Gains Like Other Post-Bear Market Troughs



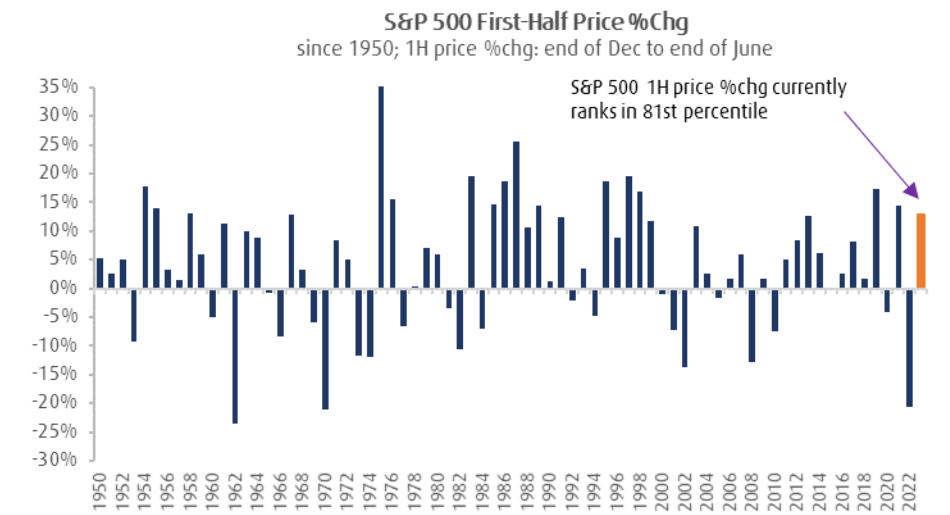
Source: BMO Investment Strategy Group, FactSet, Bloomberg.

- Admittedly we entered the year more cautious than we have been in the past given the host of uncertainties the market faced to begin 2023 (although we were still more optimistic than many of our counterparts), but it seems that all the doom and gloom that some others were prognosticating has yet come to fruition. We have always taken our cues from the data and the biggest worry entering the year was that the Fed would "hike" our economy into a severe recession. Well after 5 ppt points of rate hikes thus far, inflation has clearly subsided, and yet labor market strength has remained intact. In other words, we believe the anticipated recipe for disaster is simply not present.

- So, from our perspective, all the worries that damaged 2022 market performance are slowly beginning to subside. Yes, earnings growth is likely to remain a sticking point, but it appears investors fully understand this and are looking past 2023 results and expecting growth to reaccelerate in 2024 and beyond. Therefore, we expect market price momentum to persist, albeit at a slightly slower clip for the remainder of the year and is the reason we raised our 2023 S&P 500 year-end price target to 4,550 from 4,300. We also expect price multiple expansion to continue to drive gains as investors reset expectations as more "big risks" slowly get eliminated.

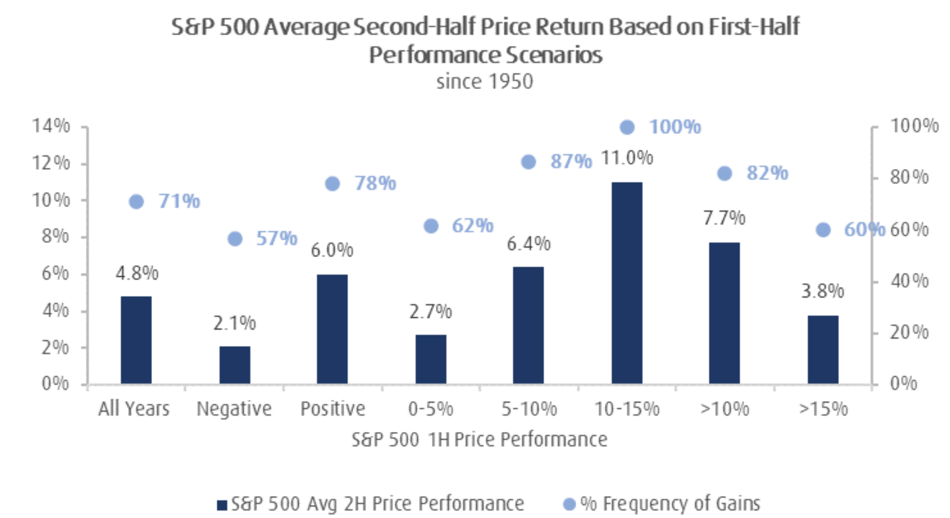
Strong Price Returns During First Half of Calendar Year Typically Lead to Further Market Gains in Second Half

SPX Has Jumped ~13% During First 6 Mos of 2023, Which Ranks in 81st Percentile



Source: BMO Investment Strategy Group, FactSet.

First-Half Gains of >10% Have Historically Been Followed by a 7.7% Avg 2H SPX Return



Source: BMO Investment Strategy Group, FactSet.

When SPX Rises 10-15% in 1H, US Stocks Post Further Gains in 2H 100% of Time

S&P 500 2H Performance During Calendar Years When 1H Price %Chg Is 10% to 15% (since 1950)

Year	First-Half S&P 500 Price %Chg	Second-Half S&P 500 Price %Chg
1955	14.0%	10.8%
1958	13.1%	22.0%
1961	11.2%	10.7%
1967	12.8%	6.4%
1985	14.7%	10.1%
1988	10.7%	1.5%
1989	14.5%	11.1%
1991	12.4%	12.4%
1999	11.7%	7.0%
2003	10.8%	14.1%
2013	12.6%	15.1%
2021	14.4%	10.9%
2023	*13.8%*	*????*
Average	**12.8%**	**11.0%**
Median	**12.7%**	**10.9%**
Prob of Gain		**100%**
Prob of >10% Gain		**75%**

Source: BMO Investment Strategy Group, FactSet.

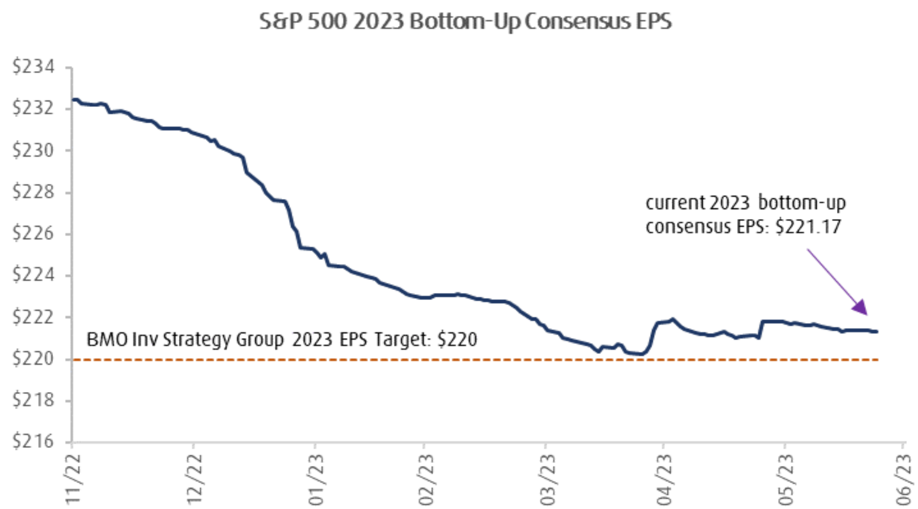
- US stocks have been extremely resilient so far in 2023 with the S&P 500 rising ~14% putting the 1H gain in the 81st percentile for all years from 1950. Yet, some investors are still calling for a sharp price drawdown in the coming months. However, our work shows that 1H starts to calendar years of this magnitude typically lead to above average 2H returns.

  ✓ For instance, there have been 13 calendar years where the S&P 500 gained 10%-15% during the 1H since 1950. The average 2H return for those years was 11%. More important, in none of those years did the S&P 500 register a 2H loss with gains ranging from 1.5% to 22%.

  ✓ In addition, a 10%-15% 1H gain appears to be the "sweet spot" as it is the only range where the average 2H gain is in double-digit territory. Furthermore, there have five 1H gains between 13%-15%, every 2H following these registered double-digit gains. Therefore, even our newly revised target could prove to be too conservative if historical trends wind up prevailing.

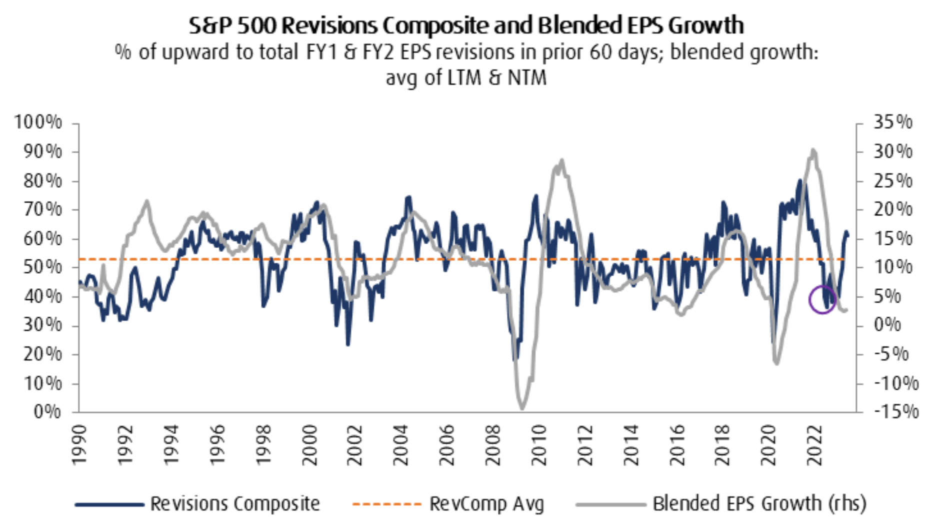
Corporate Earnings Remain Resilient

2023 Consensus Bottom-Up EPS Has Stabilized and Sits Marginally Above Our Forecast



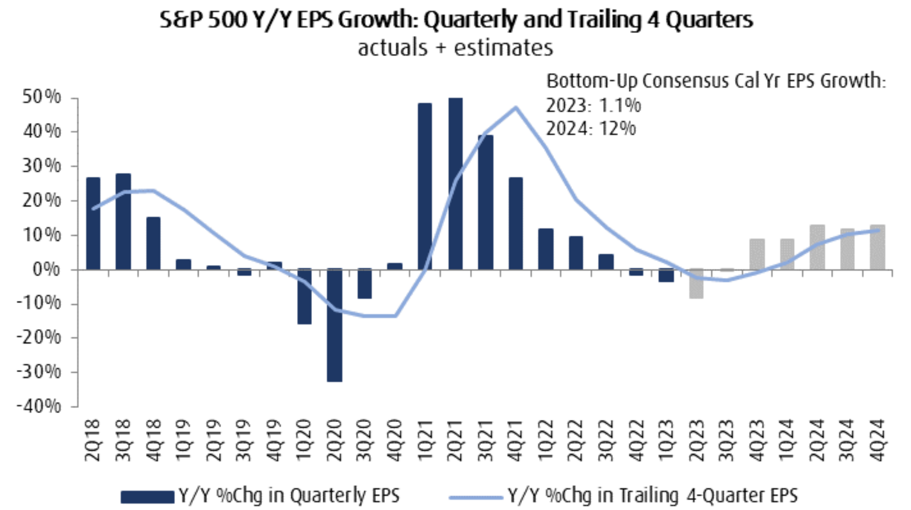
Source: BMO Investment Strategy Group, FactSet, IBES.

Upward Revisions Breadth Has Troughed, Which Should Be Positive for Blended Growth



Source: BMO Investment Strategy Group, FactSet, IBES.

Predicted Collapse in 2023 EPS Has Not Materialized With Investors Now Looking to 2024



Source: BMO Investment Strategy Group, FactSet, IBES.

- We have been a bit more cautious on the earnings outlook (although consensus has seemingly caught up) and expect 2023 S&P 500 EPS to come in roughly flat versus 2022 given the macro circumstances. Stated differently, earnings, in aggregate, are likely to see little to no growth because we believe that is what needs to happen for inflation expectations to come down (i.e., profit margin deterioration) and for the Fed to finally step aside. Fortunately, we think this is well understood by investors and believe that the market will care more about falling inflation than zero earnings growth – and maybe even more so than the prospect of a mild recession.
- Despite our own trepidation, current bottom-up consensus forecasts suggest that 2Q23 will likely represent the growth trough for this earnings cycle with a strong acceleration during 2H23 and double-digit growth expectations for 2024.
  - ✓ Revision trends appear to support this positive backdrop. According to our work, revisions and earnings growth have exhibited a strong positive relationship historically with the former typically leading the latter by several months. Therefore, the recent uptick in revisions could bode well for earnings growth in the coming months.

Sector Review and Outlook

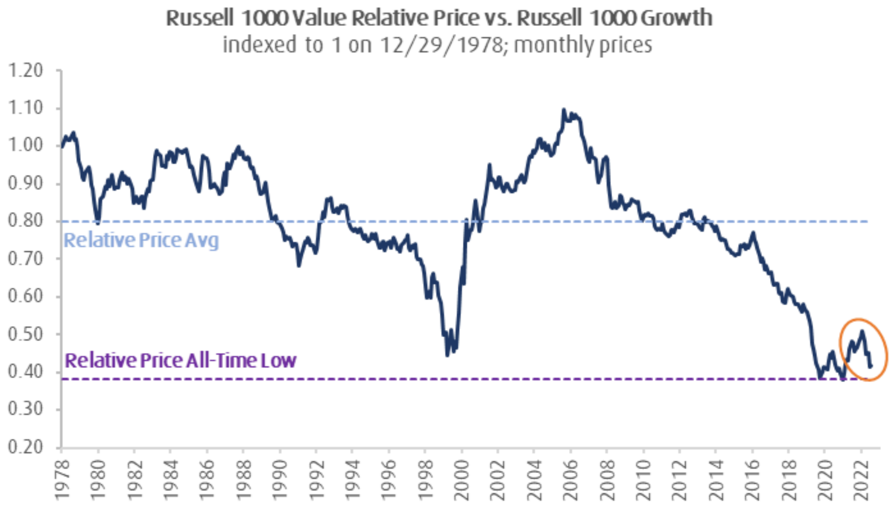
S&P 500 Sectors

Sector	Opinion	YTD Review	Our Call for 2H2023
Communication Services	OW	Second best-performing sector with key mega caps leading returns; traditional media and telecom notable laggards	Outperformance should continue, albeit at slower degree vs. 1H; quintessential barbell sector with a strong cash position and dividend growth
Financials	OW	Notable laggard as select bank failures reignited banking crisis + systemic risk fears among investors	Favorite contrarian play, remains go-to value sector; sharp price drawdown in 1H presents buying opportunity particularly given attractive valuations, dividend growth attributes, and high-quality tilt; catch-up trade for money-center banks likely
Information Technology	OW	Top performer with key mega caps leading returns; AI hype has been significant tailwind; we upgraded the group in early June	Outperformance should continue, albeit at slower degree vs 1H; Forward growth expectations have improved, and revision trends are positive; AI represents long-term tailwind
Consumer Discretionary	Mkt	Third best performing sector with AMZN + TLSA essentially leading the gains; more traditional retail groups were notable laggards	Tough to bet against US consumer especially with a still strong labor market; extended valuation could present challenges so best to be highly selective
Energy	Mkt	Sharp performance reversal from 2022 going from top to worst-performing sector alongside the slide in crude oil price	Commodity volatility likely to proceed; longer-term bullish; buy dips and focus on cash flow and dividends
Health Care	Mkt	Notable laggard as the COVID tailwind has seemingly faded away; we downgraded the group in early June	Valuations are below historical norms, but earnings growth has been a sore spot post-COVID with recent relative growth trends showing deterioration; focus on stock selection
Industrials	Mkt	Sharp June turnaround put a significant dent in YTD relative underperformance most likely driven by slightly weaker US $	Operating metrics improving but earnings growth is in a notable downtrend; focus on domestic companies and avoid internationally concentrated companies
Materials	Mkt	Like Industrials June turnaround put a significant dent in YTD relative underperformance but remains a notable laggard	Global growth volatility likely to remain elevated; focus on more defensive names with compressed valuations
Real Estate	Mkt	Interest rate environment clearly weighed on performance with group significantly underperforming	Historically performs better than other classic defensive areas in higher interest rate environments; selectivity is key, avoid commercial real estate
Consumer Staples	UW	Subsiding inflationary pressures and buoyant market gains clearly impacting the sector as it was a notable laggard	Valuation has compressed to more normalized levels, but pricing power starting to erode; focus on big brand name stocks
Utilities	UW	Logical victim of higher-for-longer interest rate environment with significant underperformance and losses	Very expensive and extremely over-owned; debt to equity levels are troublesome; own dividend growth

Source: BMO Capital Markets Investment Strategy Group; Key: OW: Overweight, MW: Market Weight, UW: Underweight

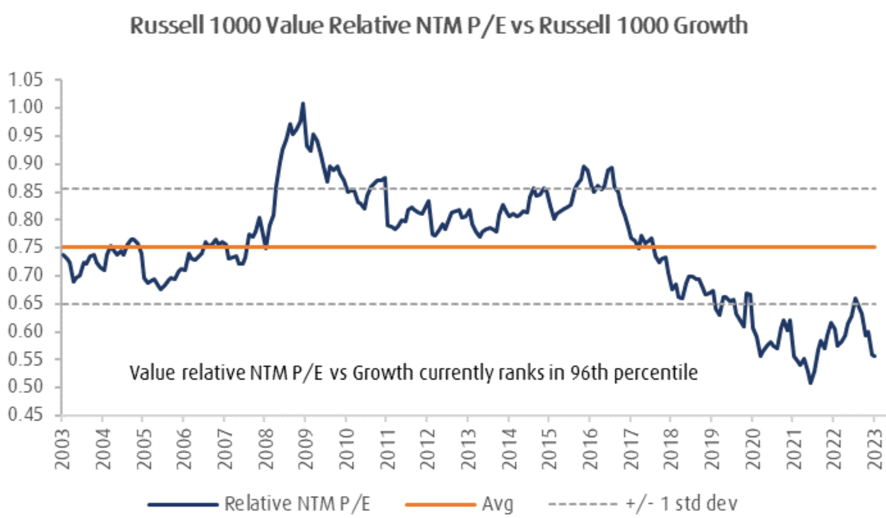
Lean Toward Value, but Also Incorporate Growth

Russell 1000 Value Relative Price vs Growth Sits ~48% Off Its Historical Monthly Average



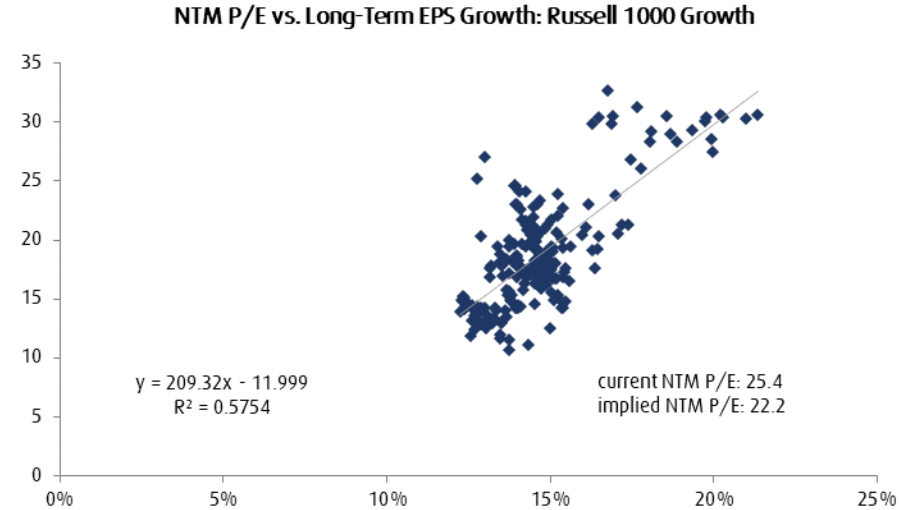
Source: BMO Investment Strategy Group, FactSet.

Value Relative NTM P/E vs Growth Is Below -1 Std Dev Level and Ranks in 96th Percentile



Source: BMO Investment Strategy Group, FactSet, IBES.

Growth NTM P/E Looks Excessive Relative to Long-Term EPS Growth Outlook



Source: BMO Investment Strategy Group, FactSet, IBES.

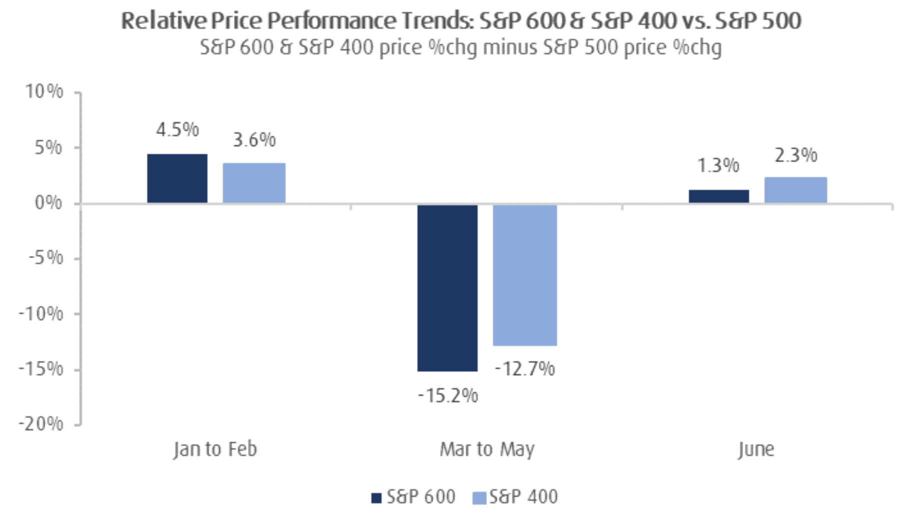
- Value stocks have been out of favor for most of this year as investors navigated back to growth-focused areas of the market, a notable shift from 2022. From our perspective, value's underperformance versus growth has been overdone with current relative price levels just marginally above historical lows.

- Nonetheless, we expect a resumption in the relative price uptrend for value in the coming months given underlying P/E and growth trends at the style level and the higher-for-longer interest rate backdrop that will likely remain in place. Therefore, as we look ahead to the rest of 2023, we continue to advise investors to maintain a value tilt in their portfolios and use periods of weakness as opportunities to add to positions in this area.

  ✓ Growth stocks have typically been more sensitive to interest rates historically. So with current multiples almost 15% higher than average given earnings growth expectations for the group, we would expect a reprice at some point once investors accept that interest rates are likely to remain higher for longer than is currently being anticipated.

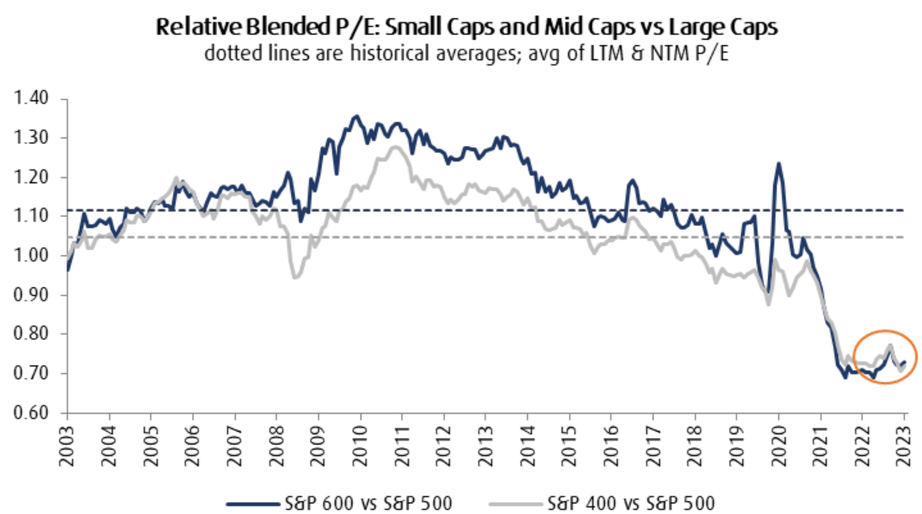
SMID-Caps Showing Signs of Life With Relative Valuations Versus Large Caps Still Near 20-Year Lows

S&P 600 & S&P 400 Have Outperformed S&P 500 Thus Far in June



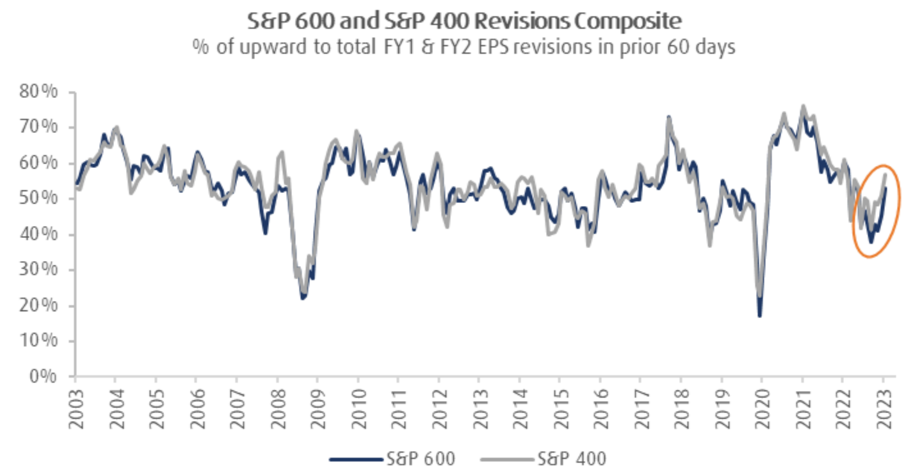
Source: BMO Investment Strategy Group, FactSet.

Small- and Mid-Cap Relative Blended P/E Ratios Sit Near 20-Year Lows



Source: BMO Investment Strategy Group, FactSet, IBES.

Percentage of Positive Annual EPS Revisions Across SMID-Caps Has Improved



Source: BMO Investment Strategy Group, FactSet, IBES.

- After notably outpacing their large-cap peers during the first two months of the year, small- and mid-cap stocks significantly underperformed in the March through May period as regional banking crisis fears sent these names tumbling. SMID-caps have been unfairly punished, in our view, and we see the excessive price downside this year as a buying opportunity for investors especially considering that the fundamental underpinnings for the group remain intact. Additionally, the group has showed signs of life in June as the S&P 600 and S&P 400 indices are both up roughly 8% month-to-date, respectively, well-ahead of the 5% S&P 500 gain.
- Relative valuations for SMID-caps vs. large caps are back down near their 20-year lows with the S&P 600 and S&P 400 carrying blended P/E ratios that are currently 27% and 28% below the S&P 500 multiple, respectively. Historically, small-cap stocks have commanded a 12% premium versus large-caps when it comes to blended P/E, while mid-cap stocks have typically traded at a 5% premium to their large-cap peers.
- On the revisions front, EPS revisions breadth seems to have already reached peak pessimism. Indeed, our S&P 600 and S&P 400 revisions composites, which track the percentage of upward FY1 & FY2 earnings revisions in the prior 60 days, troughed in January and have recently increased firmly above the 50% mark, which should be a positive signal for the earnings outlooks of these groups.

Recent US Strategy Research Reports

Date	Title
	Comments and Snapshot Reports
6/20/2023	US Strategy Comment: Remaining Market Weight Industrials for Now
6/15/2023	US Strategy Snapshot: Seasonal Performance Trends Point to Further Gains Ahead
6/5/2023	US Strategy Snapshot: S&P 500 Target Update
5/30/2023	US Strategy Snapshot: Market Resilience Does Not Necessarily Hang on Mega-Caps
5/18/2023	US Strategy Snapshot: Beneath the Surface Market Observations
5/11/2023	US Strategy Comment: Revisiting Dividend Growth
4/28/2023	US Strategy Comment: Roadmap for a Range-Bound Market
4/20/2023	US Strategy Snapshot: Earnings Recession Fears May Be Overblown
4/13/2023	US Strategy Comment: Reiterating Our Value Preference
4/5/2023	US Strategy Snapshot: Buying the Dip in Financials
3/23/2023	US Strategy Comment: Selloff in SMID-Caps Presenting a Buying Opportunity
3/17/2023	US Strategy Comment: Deploy a Barbell Strategy as Active Investing Gains Steam
3/2/2023	US Strategy Comment: Examining the Upcoming S&P GICS Changes
2/23/2023	US Strategy Snapshot: Bear Fables and Bull Facts
2/15/2023	US Strategy Snapshot: Improving Market Breadth Underpins Recent Equity Rally
2/2/2023	US Strategy Comment: Earnings Pessimism May Be Overstated
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6/6/2023	US Strategy: US Chartbook – June 2023
6/6/2023	US Strategy: US Factor Profiles – June 2023
6/6/2023	US Strategy: US Multi-Factor Profiles – June 2023
	Investment Strategy Snapshots and Special Reports
11/30/2022	2023 Market Outlook - The Year Ahead for the U.S. and Canada

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Buy	Outperform	47.8 %	18.6 %	51.8 %	53.9 %	59.8 %	57.7%
Hold	Market Perform	49.9 %	16.2 %	47.0 %	44.7 %	39.2 %	37.5%
Sell	Underperform	2.3 %	9.1 %	1.2 %	1.3 %	0.5 %	4.8%

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(April 2013 - October 2016)
http://researchglobal.bmocapitalmarkets.com/documents/2013/rating_key_2013_to_2016.pdf

(January 2010 - April 2013)
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