September 22, 2021

Canadian Strategy Snapshot

Positioning for an Epic Dividend Growth Cycle

Bottom Line: Cue the broken record… We have made it abundantly clear over the past several months – if not years – that from our perspective, a return of dividend growth and share buybacks is one of the key signs of a return to normalcy for Canadian equities. As we begin to ponder the stock market outlook for 2022 and beyond, we believe recent earnings strength places Canadian companies in a strong position to begin redeploying excess cash balances and cash flow in the form of both investments and cash distribution. In fact, the TSX has exhibited an *epic* positive surprise cycle that has translated into one of the sharpest earnings rebounds on record. This, according to our work, is likely to generate an impressive, if not ambitious dividend growth cycle that could see overall dividend growth surge well above historical averages over the next 12-24 months. As such, we believe investors should begin positioning in areas that are likely to increase dividends and share buybacks.

Main Points:

- Dividend Growth Poised for Epic Rebound Into 2022
  - ✓ Blockbuster earnings surprise + record earnings rebound + excess cash = suggests to us that the TSX could see one of the strongest periods of dividend growth in decades as we head into 2022.
- Cyclical Areas Key to Dividend Growth
  - ✓ Cyclical areas like Consumer Discretionary, Financials, and Industrials have seen their dividend growth slow sharply over the last twelve months, despite posting one of the strongest earnings rebounds on record.
- Consumer Discretionary Aligned for Strong Dividend Growth
  - ✓ Despite some near-term supply chain concerns, we believe the Consumer Discretionary sector has many of the hallmarks of a dividend growth sector and is likely going to be one of the key areas of dividend growth in the TSX over the next 12-24 months.
- Financials Could See Highest Dividend Growth Rate in a Decade
  - ✓ Our work suggests a significant amount of pent up dividend growth within Financials.
- Industrials Has Competing Uses of Cash
  - ✓ The Industrial sector's cash position remains strong and poised for deployment. However, we believe the hierarchy of capital deployment will likely focus on capex and M&A, followed by share buybacks and then renewed dividend growth.

Implementation Strategies: North American Dividend Growth Portfolio

For disclosure statements, including the Analyst Certification, please refer to page(s) 9 to 11.

BMO Capital Markets

Investment Strategy

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CDN Strategy – S&P/TSX Targets

S&P/TSX Price Target	
2021 Calendar Year End	22,000

S&P/TSX EPS Target	
2021 Calendar Year End	$1400

Source: BMO Capital Markets Investment Strategy.

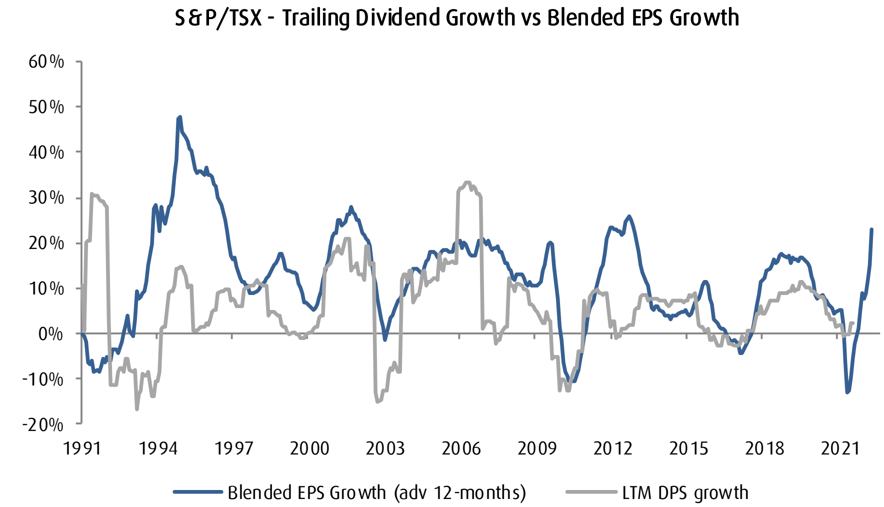
CDN Strategy – Recommended S&P/TSX Sector Weightings

Sector	Opinion	Tgt. Wgt.
Communication Services	MW	5.0%
Consumer Discretionary	OW	5.0%
Consumer Staples	MW	4.0%
Energy	MW	11.0%
Financials	OW	31.0%
Health Care	MW	1.5%
Industrials	OW	13.5%
Information Technology	MW	9.5%
Materials	OW	14.5%
Real Estate	UW	3.0%
Utilities	UW	2.0%

Source: BMO Capital Markets Investment Strategy.
OW: Overweight
MW: Market Weight
UW: Underweight

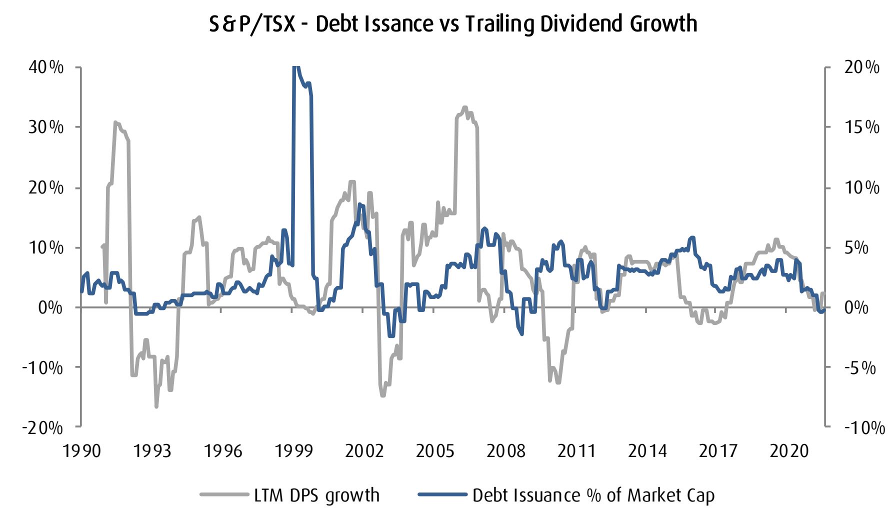
Dividend Growth Poised for Epic Rebound Into 2022

Dividend Growth Is Poised for Strong Rebound Over Next Twelve Months



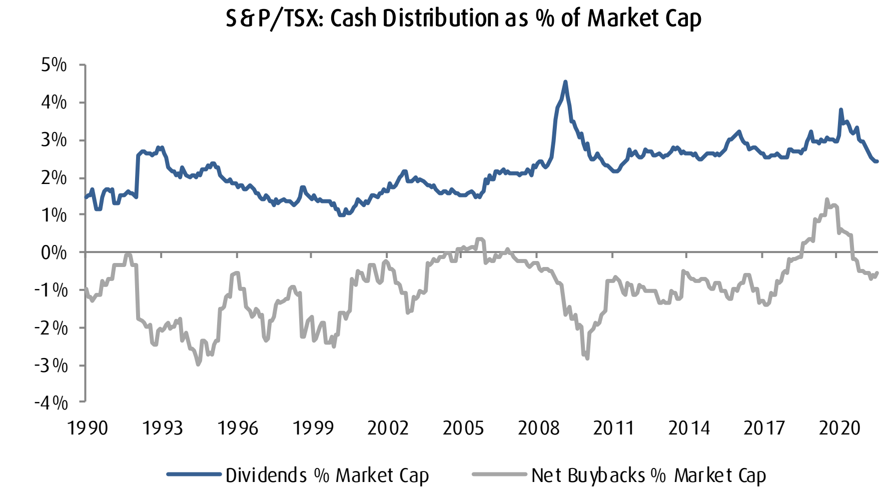
Source: BMO Capital Markets Investment Strategy Group, FactSet, Compustat, IBES.

Rebound in Debt Issuance would be Supportive of Rebounding Dividend Growth



Source: BMO Capital Markets Investment Strategy Group, FactSet, Compustat, IBES.

Cash Distribution Has Declined as Percent of Market Cap



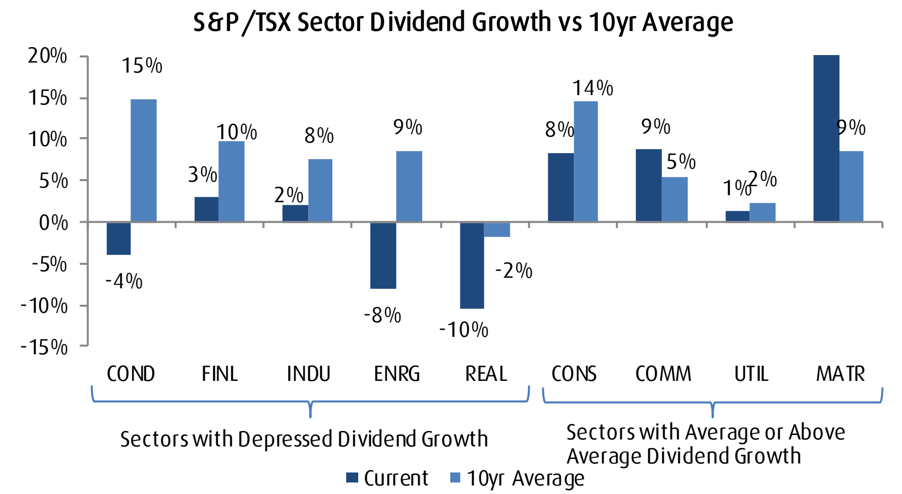
Source: BMO Capital Markets Investment Strategy Group, FactSet, Compustat, IBES.

We have made it abundantly clear over the past several months – if not years – that from our perspective, a return of dividend growth and share buybacks is one of the key signs of a return to normalcy for Canadian equities. In fact, dividend and cash distribution was a significant area of concern in the early part of the pandemic, with dividend strategies significantly underperforming in 2020. Furthermore, corporations shifted to a more defensive cash preservation mode with companies cutting investment spending and slowing distribution growth while building cash balances. As we begin to ponder the 2022 outlook, we believe recent earnings strength places Canadian companies in a strong position to begin redeploying excess cash balances and cash flow in the form of both investments and cash distribution.

- Our blended EPS growth model tends to lead dividend growth by up to twelve months, suggesting the TSX could see one of the strongest periods of dividend growth in decades.
- Furthermore, the lack of debt issuance over the last twelve months suggests to us that there is more cash available for capex, M&A, and distributions than suggested by the strong cash on balance sheet and free cash flow. Indeed, rebound in debt issuance is historically supportive of rebounding dividend growth.

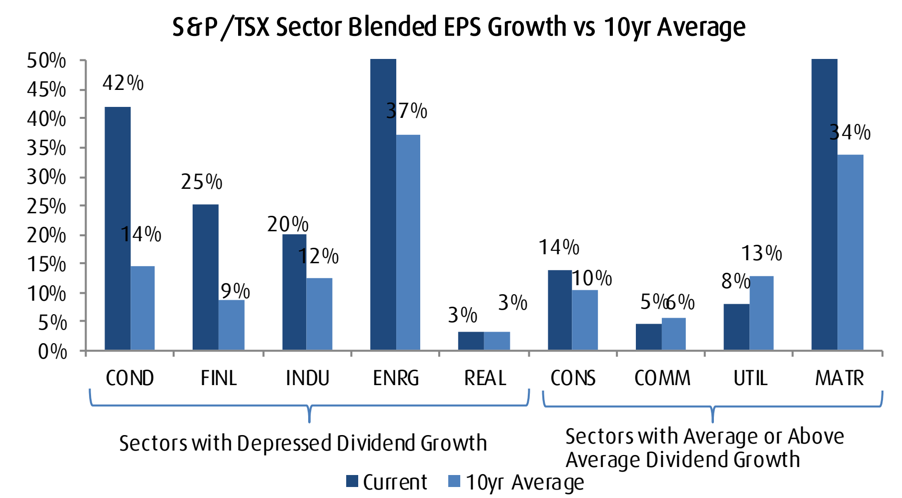
Cyclical Areas Key to Dividend Growth

Cyclical Sectors Have Most Depressed Dividend Growth



Source: BMO Capital Markets Investment Strategy Group, FactSet, Compustat, IBES.

Cyclical Areas Have Seen Sharpest Earnings Rebound



Source: BMO Capital Markets Investment Strategy Group, FactSet, Compustat, IBES.

While we expected dividend growth to surge above historical averages over the next 12-24 months, much of the rebound will likely occur due to companies normalizing historical dividend growth rates. Therefore, when looking for areas that are most likely to see the strongest dividend growth in the near term, we tend to prefer those areas that moved to more defensive, cash preservation strategies during the pandemic. In fact, when we compare current dividend growth rates of sectors to the 10-year average, we can see the more defensive areas of the market generally maintained historical dividend growth rates, while the more cyclical areas have posted dividend growth rates well below the average.

- Cyclical areas like **Consumer Discretionary, Financials, and Industrials** have seen their dividend growth slow sharply over the last twelve months, despite posting one of the strongest earnings rebounds on record. As such, we believe these are key areas that are likely to see above average dividend growth over the next 12-months as companies begin to return excess cash to shareholders.

- While the **Energy** sector has certainly seen one of the sharpest drops in distribution, we continue to believe these more defensive corporate actions remains a prudent strategy given the headwinds of the sector.

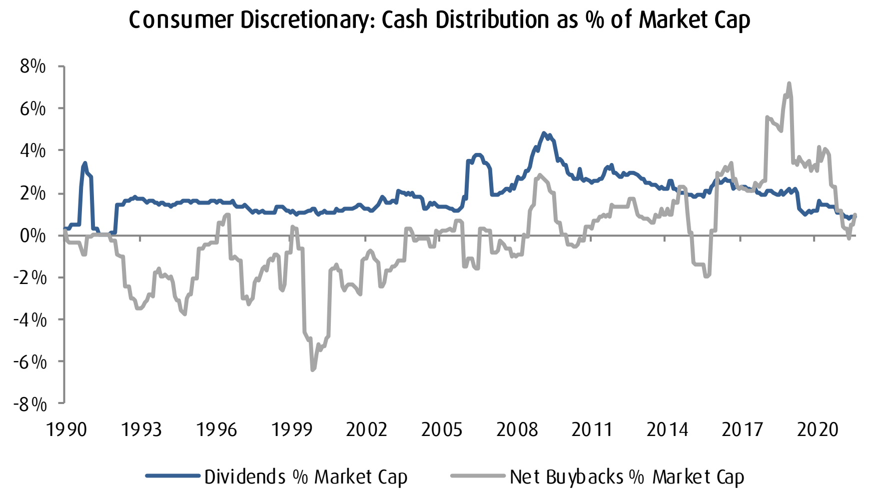
- In our opinion, while being selective by segment is paramount, the broad **Real Estate** sector may face some headwinds in restoring dividends despite being a strong re-opening trade. Yes, we believe work from home and new variants continue to point to fits and starts to restoring consistent dividend growth in the near term, particularly for the office and retail segments.

- **Consumer Staples, Communication Services, and Utilities** have all seen dividend growth rates largely in line with their 10-year averages. As such, we believe these sectors are likely to just maintain dividend growth rates, and not likely to be a major source of incremental dividend growth.

- **Materials** has been one of the only sectors to see dividend growth over the last twelve months meaningfully exceed its historical average. Given continued elevated commodity prices, we believe dividend growth will likely continue, albeit at a slower rate in our opinion.

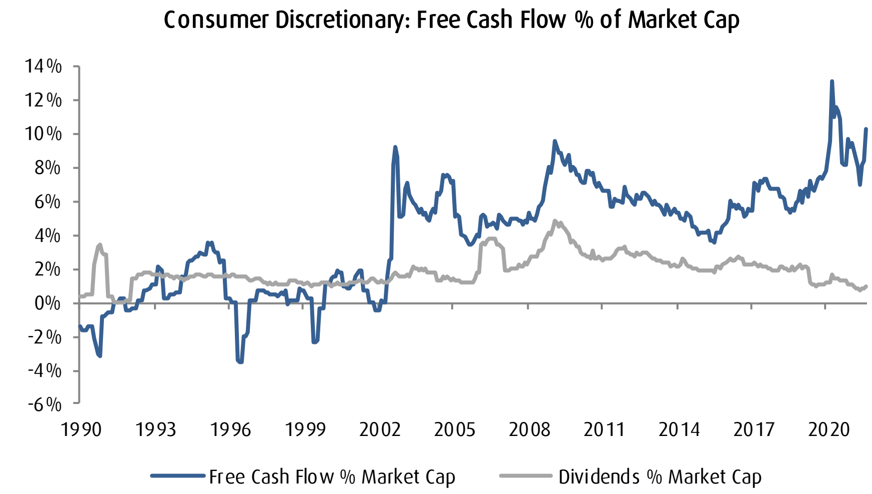
Consumer Discretionary Aligned for Strong Dividend Growth

Consumer Discretionary Has Seen Distribution Compression



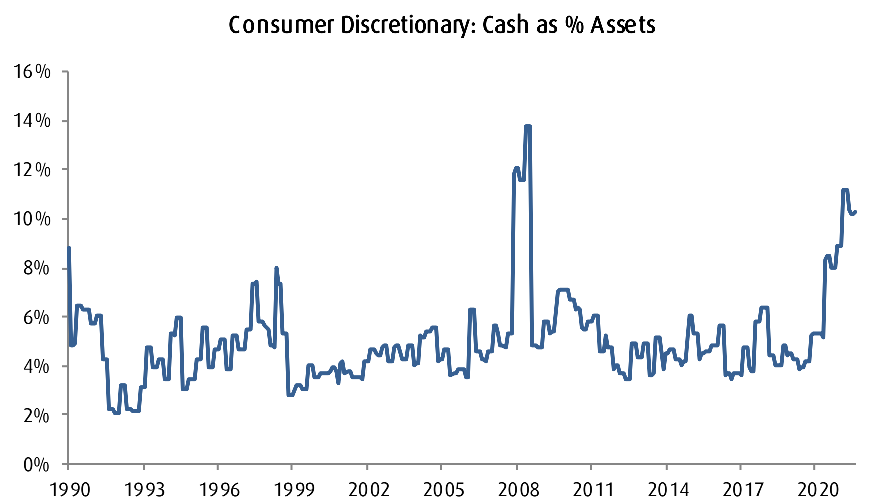
Source: BMO Capital Markets Investment Strategy Group, FactSet, IBES, Compustat.

Yet, Free Cash Flow Coverage Is at a Record Level



Source: BMO Capital Markets Investment Strategy Group, FactSet, IBES, Compustat.

And Cash on Balance Sheet at Near Record Levels



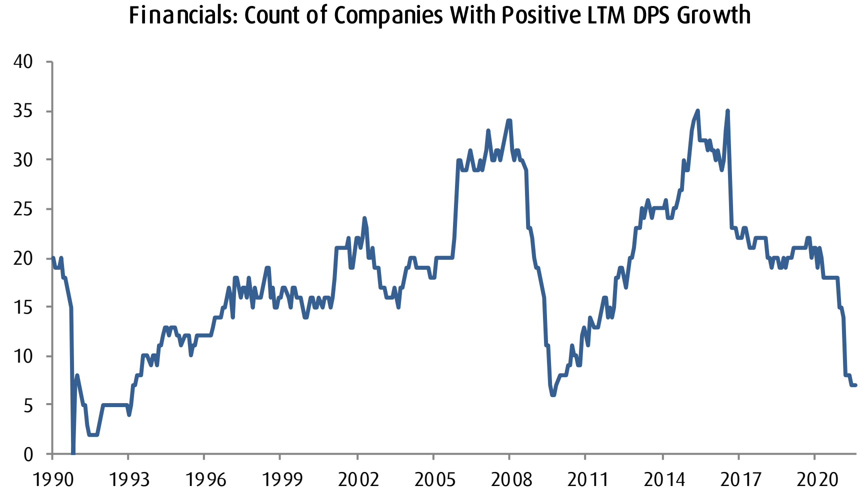
Source: BMO Capital Markets Investment Strategy Group, FactSet, IBES, Compustat.

No doubt supply chain concerns remain a key headwind for the sector and a reason for some companies, particularly the automotive industry, to remain cash flow cautious. However, Consumer Discretionary stocks have already seen cash distribution levels compress to the lowest levels in almost 10 years, with dividend and buybacks as a percentage of market cap falling below 1% and well below the historical average.

Overall, fundamentally many of the stars have aligned for the sector to post some of the strongest dividend growth rates on record. Free cash flow yield has surged to the highest level on record and now has the largest spread versus dividend yield since 1990. Furthermore, the sector has accumulated one of the strongest cash balances on record, which we believe almost certainly raises the pressure on companies to begin returning excess cash to shareholders. This is all in addition to the fact the sector has posted one of the strongest earnings rebound on record that continues to defy even the most optimistic estimates. As such, despite some near-term supply chain concerns, we believe the Consumer Discretionary sector is going to be one of the key areas of dividend growth in the TSX over the next 12-24 months.

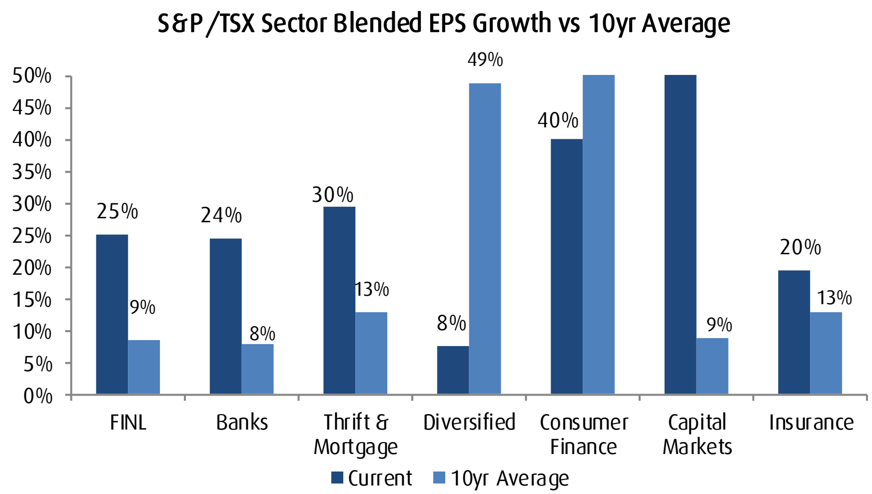
Financials Could See Highest Dividend Growth Rate in a Decade

Canadian Financials Have Lowest Number of Companies Raising Dividends Since 2009



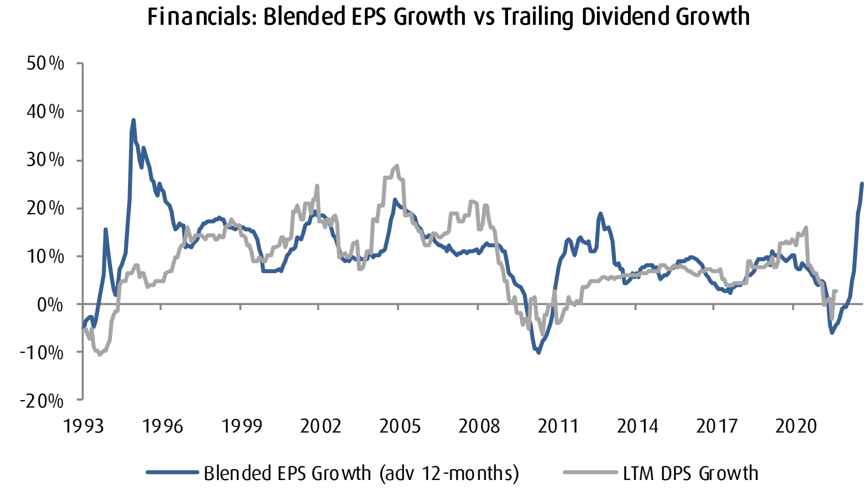
Source: BMO Capital Markets Investment Strategy Group, FactSet, Compustat, IBES.

Earnings Rebound Broad Based... With Banks Leading the Way



Source: BMO Capital Markets Investment Strategy Group, FactSet, Compustat, IBES.

Financials Could See Double Digit Dividend Growth Heading Into 2022



Source: BMO Capital Markets Investment Strategy Group, FactSet, Compustat, IBES.

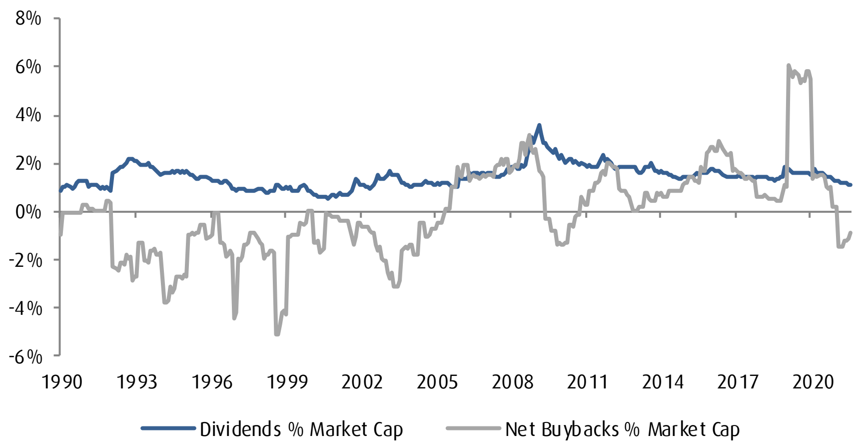
Outside of the impact of the Energy sector, the Financial sector has been the largest drag on overall S&P/TSX dividend growth over the last year. Indeed, the Canadian Financial sector has the lowest number of companies since 2009 that are posting positive year-over-year dividend growth. Unlike 2008, when the recession was centered around Financial stability and liquidity, the current pullback in dividend growth is largely due to cautionary and temporary regulatory restrictions that are looking increasingly unnecessary at this point in the cycle, particularly as the market and the Financial sector has posted one of the strongest earnings recoveries since the 1990's. Overall, our work suggests a significant amount of pent-up dividend growth within Financials. As such, we believe this sector is likely to be the largest source of dividend growth over the next 12-24-months and may reach the highest rate of growth in a decade.

- Financials earnings growth is highly correlated with dividend growth, suggesting a significant amount of pent-up dividend growth over the next 12-24 months.
- The earnings rebound has been broad, with Banks, Mortgage companies, Capital Markets, and Insurance companies all poised for above-average dividend growth.

Industrials Has Competing Uses of Cash

While Dividend Growth Has Slowed, Industrials Saw a Sharp Drop in Buybacks

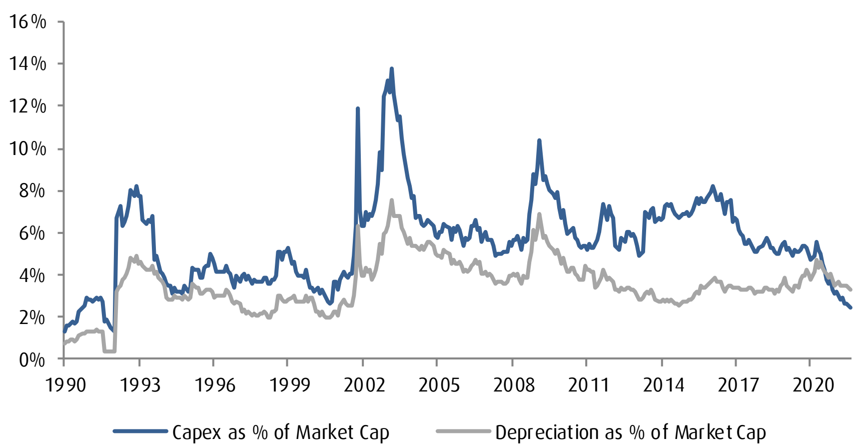
Industrials: Cash Distribution as % of Market Cap



Source: BMO Capital Markets Investment Strategy Group, FactSet, IBES, Compustat.

Capital Spending and M&A Likely to Be Key Areas of Cash Deployment

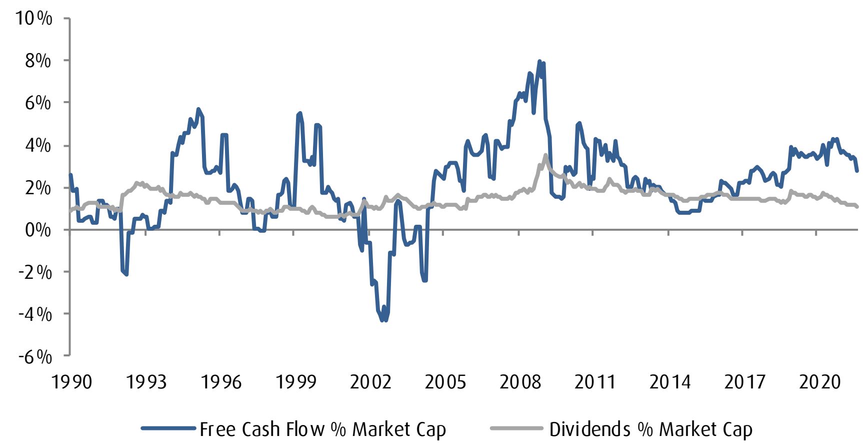
Industrials: Capex as % of Market Cap



Source: BMO Capital Markets Investment Strategy Group, FactSet, IBES, Compustat.

Industrial Free Cash Flow Is Strong but Not Near Record

Industrials: Free Cash Flow as % of Market Cap



Source: BMO Capital Markets Investment Strategy Group, FactSet, IBES, Compustat.

While we certainly believe the Industrial sector is well positioned for a rebound in dividend growth, unlike Consumer Discretionary and Financials, we believe Industrials likely has more competing interests in uses of cash. In fact, the largest pullback in distributions was in net buybacks, which has turned to net new equity issuance for the first time since 2010. As such, this is likely the first area that will see cash distribution in our opinion. Additionally, Industrials has seen one of the sharpest pullbacks in capital spending, which has even fallen below the rate of depreciation, suggesting the sector likely needs to increase investment capital before focusing on cash distribution.

Overall, the Industrial sector's cash position remains strong and poised for deployment. However, the rebound has not been as strong as Consumer Discretionary or Financials and much of the strength in free cash flow has come from a pullback in capital spending. As such, we believe the hierarchy of capital deployment will likely focus on capex and M&A, followed by share buybacks and then renewed dividend growth. Therefore, investors should be selective from a dividend growth perspective, in our opinion.

Implementation Strategies: North American Dividend Growth Portfolio

Ticker	Company	Price	BMO Rating
AAPL	Apple Inc.	143.43	NR
AMGN	Amgen Inc.	215.36	NR
AMP	Ameriprise Financial, Inc.	253.5	NR
AQN-CA	Algonquin Power & Utilities Corp.	19.47	Mkt
BAC	Bank of America Corp	39.13	Mkt
BCE-CA	BCE Inc.	64.89	OP
BIP.UT-CA	Brookfield Infrastructure Partners L.P.	69.81	OP
BLK	BlackRock, Inc.	845.24	Mkt
C	Citigroup Inc.	66.94	OP
CMCSA	Comcast Corporation Class A	56.06	NR
CNR-CA	Canadian National Railway Company	147.61	Mkt
CSCO	Cisco Systems, Inc.	55.26	NR
EMN	Eastman Chemical Company	99.18	NR
ENB-CA	Enbridge Inc.	50.28	OP
GD	General Dynamics Corporation	191.19	NR
GILD	Gilead Sciences, Inc.	71.73	Mkt
GS	Goldman Sachs Group, Inc.	375.84	OP
IP	International Paper Company	55.22	OP
JNJ	Johnson & Johnson	164.53	NR
JPM	JPMorgan Chase & Co.	152.98	Mkt
LMT	Lockheed Martin Corporation	336.05	NR
LOW	Lowe's Companies, Inc.	206.27	NR
MCD	McDonald's Corporation	240.5	OP
MFC-CA	Manulife Financial Corporation	23.67	OP
MRK	Merck & Co., Inc.	71.97	NR
MS	Morgan Stanley	98.3	OP
MSFT	Microsoft Corporation	294.8	OP
PEP	PepsiCo, Inc.	153.54	NR
PG	Procter & Gamble Company	143.11	NR
POW-CA	Power Corporation of Canada	42.52	Mkt
PPL	PPL Corporation	28.42	NR
QSR-CA	Restaurant Brands International Inc	79.81	OP
RY-CA	Royal Bank of Canada	125.33	Mkt
T	AT&T Inc.	26.96	NR
T-CA	TELUS Corporation	28.71	OP
TD-CA	Toronto-Dominion Bank	82.1	Mkt
TRP-CA	TC Energy Corporation	61.77	OP
TXN	Texas Instruments Incorporated	192.96	OP
UNH	UnitedHealth Group Incorporated	412.34	Mkt
VZ	Verizon Communications Inc.	54.03	NR
WM	Waste Management, Inc.	152.75	OP

Source: BMO Capital Markets Investment Strategy. Prices as of 9/21/2021.

*Rating Key, according to BMO Capital Markets Equity Research: OP: Outperform, Mkt: Market Perform, Und: Underperform, NR: Not rated by BMO Capital Markets Equity Research.

Canadian Strategy Research Reports

Date	Title
	Canadian Strategy Snapshots
9/16/2021	Canadian Strategy Snapshot: Dissecting the Canadian Value Proposition
8/30/2021	Canadian Strategy Snapshot: Raising 2021 Targets Amid Another Blowout Quarter
8/19/2021	Canadian Strategy Snapshot: Sometimes Two Out of Three Is Not Enough
7/29/2021	Canadian Strategy Snapshot: Communications Remains Preferred Yield Sector
7/22/2021	Canadian Strategy Snapshot: Small Cap Opportunities Persist
7/15/2021	Canadian Strategy Snapshot: Three Insights From Recent Market Strength
6/25/2021	Canadian Strategy Snapshot: 2021 Mid-Year Outlook
6/17/2021	Canadian Strategy Snapshot: Defensive Corporations Turning to Offense
6/10/2021	Canadian Strategy Snapshot: Positive Revision and Surprise Tailwinds to Prevail
5/27/2021	Canadian Strategy Snapshot: Reactionary Revisions Chasing Positive Surprises
5/20/2021	Canadian Strategy Snapshot: Divergent Performance in Materials Set to Converge
5/11/2021	Canadian Strategy Snapshot: Raising Our 2021 S&P/TSX Price and EPS Targets
4/28/2021	Canadian Strategy Snapshot: Debunking Seasonality and Other Bearish Concerns
4/22/2021	Canadian Strategy Snapshot: Consumer Staples for Tactical Defense
4/6/2021	Canadian Strategy Snapshot: Three First Quarter Performance Observations
	Monthly Reports
9/7/2021	Canadian Strategy: Canadian Chartbook – September 2021
9/7/2021	Canadian Strategy: Canadian Factor Profiles – September 2021
	Podcasts
7/16/2021	Podcast - 2021 Mid-Year Update
1/26/2021	Podcast - COVID-19: The Biden Presidency and What Lies Ahead
12/15/2020	Podcast - COVID-19: What Comes Next
11/20/2020	Podcast - 2021 Market Outlook – The Year Ahead for the U.S. and Canada
11/9/2020	Podcast - Charting Investment in a Biden Presidency
11/4/2020	Podcast - Early U.S. Election Results: What We Know
6/30/2020	Podcast - Recession Recedes Even as U.S. Infections Surge
5/27/2020	Podcast - Tracking a Vaccine
5/20/2020	Podcast - Testing the Depths of the COVID Recession
5/12/2020	Podcast - Mission Critical – Testing Testing
	Investment Strategy Snapshots and Special Reports
11/19/2020	Investment Strategy: 2021 Market Outlook
11/19/2020	Canadian Strategy Snapshot: 2021 Year Ahead – Canadian Market Outlook
	US Strategy
	Please call or e-mail us to be added to our standalone US Strategy research

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Distribution of Ratings (September 21, 2021)

Rating category	BMO rating	BMOCM US Universe*	BMOCM US IB Clients**	BMOCM US IB Clients***	BMOCM Universe****	BMOCM IB Clients*****	StarMine Universe~
Buy	Outperform	51.8 %	29.4 %	58.3 %	54.0 %	60.7 %	57.7%
Hold	Market Perform	47.3 %	22.3 %	40.3 %	45.0 %	38.6 %	37.5%
Sell	Underperform	0.9 %	40.0 %	1.4 %	1.1 %	0.6 %	4.8%

* Reflects rating distribution of all companies covered by BMO Capital Markets Corp. equity research analysts.

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OP = Outperform - Forecast to outperform the analyst’s coverage universe on a total return basis;
Mkt = Market Perform - Forecast to perform roughly in line with the analyst’s coverage universe on a total return basis;
Und = Underperform - Forecast to underperform the analyst’s coverage universe on a total return basis;
(S) = Speculative investment;
Spd = Suspended - Coverage and rating suspended until coverage is reinstated;
NR = No Rated - No rating at this time; and
R = Restricted - Dissemination of research is currently restricted.

The total return potential, target price and the associated time horizon is 12 months unless otherwise stated in each report. BMO Capital Markets' seven Top 15 lists guide investors to our best ideas according to different objectives (CDN Large Cap, CDN Small Cap, US Large Cap, US Small Cap, Income, CDN Quant, and US Quant have replaced the Top Pick rating).

Prior BMO Capital Markets Rating System

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

(January 2010 - April 2013)
http://researchglobal.bmocapitalmarkets.com/documents/2013/prior_rating_system.pdf

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