

Canadian Equity Markets:

The TSX index has recovered most of its losses since the peak in late February and is now down only 0.3% on the year. With announcements of the vaccines progress on Nov. 9th the TSX energy index (made up of oil & gas producers) has rallied 25% and the more influential financials index (banks and insurance Cos.) is up 12%; contributing to an overall 3% rise in the index. Declining gold prices dampened the overall effect. The recent bank and life insurance gains, while impressive, leave these sectors still down on the year with dividend yields averaging in the 4% - 5% range. The banks in particular are benefiting from two main factors, firstly an expectation of lower write-offs in 2021 and secondly, an increase in 5 and 10 year yields in the past two weeks leading to a steeper yield curve. While short term funding costs remain low, this steepening of the yield curve will improve the net spread on loans, thereby enhancing bank profits. The Canadian banks report Q4 earnings the first week of December and we expect the analysts will comment on 2021 more clearly. Our view is that given the current low valuations, high dividend yields and expected earnings improvement in 2021, the Canadian banking sector could perform well in 2021. We continue to hold TD, Royal Bank and Manulife and would add to these names where we are underweight. Other sectors which have rallied, although in a more restrained fashion, are the telecom and pipeline sectors, although still down in 2020. Given yields in the 3% - 6% range and further dividend growth for these sectors, combined with attractive valuations, we would continue to hold TC Energy (N.A.'s largest gas pipeline company) and Rogers Communications. Other holdings making up our Canadian equity model are CNR, Fortis, Brookfield Asset Management, Franco Nevada (gold streaming company) and we recently added Brookfield Renewable Energy

US Equity Markets:

To the surprise of many sceptics the US S&P 500 index has rallied 10% in 2020. However also as widely observed, the rally is based almost solely on the dominant technology sector (comprising ~40% of the total) climbing ~36% in 2020. A combination of resilient earnings, investors fleeing other sectors and the valuation benefit of sharply declining interest rates, have only enhanced the market strength of this already most influential sector. Looking ahead we expect that the non Tech sectors of banking, consumer, pharma and industrial (where we also hold exposure), to recover along with the more trodden down sectors of real estate and travel (sectors we are largely not in) to recover over the next 1 – 2 years.

Our equity US holdings are: Alphabet, Amazon, MasterCard, JP Morgan, Disney, Johnson & Johnson, Raytheon and the Vanguard Tech ETF symbol "VGT." At the margin we are increasing positions in the non Tech sectors.

US and Canadian Fixed Income Markets:

Central Bank interest rates were cut sharply in the US and Canada during the onset of the pandemic in March and remain at levels just above zero, although 5 and 10 year yields have ticked up slightly with the news of the vaccines. As rates came down, bond prices rose generating year to date returns in the mid-term bond markets of 7 – 8%. For the traditional 60/40; equity/bond portfolios, both the bond and equity markets delivered positive returns with bonds largely playing their expected role of offsetting and dampening the swings in the equity markets during 2020. However with government yields now below 1% (even for 10 year maturities) the future returns in bonds are likely at best to be modest, if positive at all.

Preferred shares, which disappointed investors for the past few years, are likely to offer greater returns than bonds in the future. The market is strongly influenced by the rate reset preferred shares which underperform in a

declining interest rate environment. We have commented previously in greater detail but in summary; rate reset preferred shares fall in reaction to declining rates and rise (absent any credit quality issues) when interest rates go up, although recent interest rate increases have been rare. Given the relatively illiquid preferred market vs. a much deeper bond market, these price moves tend to be exaggerated. We continue to hold C\$ and US\$ preferred shares as a component of our fixed income allocation and believe they will offset in part the effect of rising rates on the bond markets.

2021 Outlook:

We have had a lot of news flow lately, with a US election that is largely behind us leading to a divided congress (to some degree), and the news of two vaccines for COVID-19 that seems will be largely effective. This has all given us some more confidence that earnings will start getting back to normal in the next 6-12 months. This is not to say that there aren't potential curve balls going forward from the technologies of the new vaccines to a new relationship to be formed between Canada and the US, but directionally the news has been positive.

The big picture view is that we are coming out of a recession, and GDP should grow in North America at a strong clip off the lows with Europe following after. China has already regained all the lost ground from the pandemic. Though multiples are high and some would argue that the market is 'overvalued', we see the high index valuations as being a function of really one sector, technology, that has lower earnings on average but tremendous earnings growth making up ~40% of the S&P 500. We believe that earnings of the companies we hold in the portfolios will rebound in time and we have conviction that the prices will trend higher with that, the multiples may not grow or may even shrink slightly but that in turn would give us further confidence.

That being said at this time we are not increasing equity allocations beyond our targets, and will continue to advocate a defensive bias among the equities we hold, as well and a balance/diversification among asset classes of gold and fixed income a hedge as though much big news is behind us – it doesn't mean that the volatility will certainly stop.

Sources: Bloomberg, JP Morgan, Thomson & BMO Nesbitt Burns research. We deliver a full complement of thoughtful, customized wealth solutions for private clients and institutions, drawing upon global resources, top ranked research and the collective wisdom of BMO Nesbitt Burns and our internal and external partners. For more information on our team we invite you to contact us.

Cecil Hayhoe
Portfolio Manager &
Investment Advisor
416-359-5361
cecil.hayhoe@nbpcd.com

Gwyneth Pryse-Phillips
Portfolio Manager &
Investment Advisor
416-359-5384
gwyneth.pryse-phillips@nbpcd.com

Adeel Yusoof
Investment Representative
416-359-8296
adeel.yusoof@nbpcd.com

BMO Nesbitt Burns | 2 St. Clair Avenue West. | 19th Floor | Toronto, ON M4V 1L5

Member-Canadian Investor Protection Fund

Member of the Investment Industry Regulatory Organization of Canada.

*Disclaimers: BMO Wealth Management is the brand name for a business group consisting of Bank of Montreal and certain of its affiliates in providing wealth management products and services ®"BMO (M-bar roundel symbol)" is a registered trade-mark of Bank of Montreal, used under licence.

® "Nesbitt Burns" is a registered trade-mark of BMO Nesbitt Burns Inc. BMO Nesbitt Burns Inc. is a wholly-owned subsidiary of Bank of Montreal. The opinions, estimates and projections contained herein are those of the author as of the date hereof and are subject to change without notice and may not reflect those of BMO Nesbitt Burns Inc. ("BMO NBI"). Every effort has been made to

ensure that the contents have been compiled or derived from sources believed to be reliable and contain information and opinions that are accurate and complete. Information may be available to BMO Nesbitt Burns or its affiliates that is not reflected herein. However, neither the author nor BMO NBI makes any representation or warranty, express or implied, in respect thereof, takes any responsibility for any errors or omissions which may be contained herein or accepts any liability whatsoever for any loss arising from any use of or reliance on this report or its contents. This report is not to be construed as an offer to sell or a solicitation for or an offer to buy any securities. BMO NBI, its affiliates and/or their respective officers, directors or employees may from time to time acquire, hold or sell securities mentioned herein as principal or agent. BMO Nesbitt Burns Inc. and BMO Nesbitt Burns Ltee/Ltd. ("BMO Nesbitt Burns") will buy from or sell to customers' securities of issuers mentioned herein on a principal basis. BMO Nesbitt Burns, its affiliates, officers, directors or employees may have a long or short position in the securities discussed herein, related securities or in options, futures or other derivative instruments based thereon. BMO Nesbitt Burns or its affiliates may act as financial advisor and/or underwriter for the issuers mentioned herein and may receive remuneration for same. A significant lending relationship may exist between Bank of Montreal, or its affiliates, and certain of the issuers mentioned herein. BMO NBI is a wholly owned subsidiary of BMO Nesbitt Burns Corporation Limited which is a majority-owned subsidiary of Bank of Montreal. Any U.S. person wishing to effect transactions in any security discussed herein should do so through BMO Nesbitt Burns Corp. and/or BMO Nesbitt Burns Securities Ltd. Member-Canadian Investor Protection Fund.