Asset Allocation ETFs: An important decision, simplified

Diversification through asset classes: By investing in only one asset class you may miss out on potential gains.

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Highest Return	CE 17.6%	CB 9.7%	EE 17.3%	USE 41.3%	USE 23.9%	USE 21.6%	CE 21.1%	EM 28.7%	USE 4.2%	USE 24.8%	EM 16.9%
	EM 13.0%	GB 6.5%	EM 16.0%	EE 34.4%	BP 11.6%	IE 19.5%	USE 8.1%	EE 17.9%	GB 1.9%	CE 22.9%	USE 16.5%
	USE 9.1%	USE 4.6%	IE 15.3%	IE 31.6%	CE 10.6%	EE 17.1%	EM 7.7%	IE 17.4%	CB 1.4%	EE 18.3%	BP 10.5%
	BP 8.8%	BP 1.1%	USE 13.4%	BP 16.5%	GB 9.4%	BP 7.6%	BP 6.6%	USE 13.8%	C 1.4%	IE 16.5%	CB 8.7%
	CB 6.7%	C 1.0%	BP 8.5%	CE 13.0%	CB 8.8%	CB 3.5%	GB 3.5%	CE 9.1%	BP -1.2%	BP 16.1%	GB 7.0%
	GB 3.8%	EE -8.3%	CE 7.2%	EM 4.3%	EM 7.0%	EM 2.4%	CB 1.7%	BP 8.8%	IE -5.6%	EM 12.9%	IE 6.6%
	IE 2.6%	CE -8.7%	GB 5.3%	C 1.0%	IE 4.1%	GB 1.9%	C 0.5%	CB 2.5%	EM -6.5%	CB 6.9%	CE 5.6%
	C 0.5%	IE -9.5%	CB 3.6%	GB 1.0%	EE 2.8%	C 0.6%	IE -2.0%	GB 1.8%	EE -6.6%	GB 6.9%	EE 4.1%
Lowest Return	EE -1.0%	EM -16.1%	C 1.0%	CB -1.2%	C 0.9%	CE -8.3%	EE -3.2%	C 0.6%	CE -8.9%	C 1.6%	C 0.9%

Source: Morningstar Direct. All returns in C$ and are calendar year returns.
Past performance is not indicative of future results.

IE	**International Equities** MSCI EAFE Index
USE	**U.S. Equities** S&P 500 Total Return Index
CE	**Canadian Equities** S&P/TSX Composite Index
CB	**Canadian Bonds** FTSE TMX Canada Universe Bond Index
C	**Cash** FTSE TMX Canada 91 Day T-Bill Index
GB	**Global Bonds** Citi World Government Bond
EE	**European Equities** MSCI Europe Total Return Index
EM	**Emerging Market Equities** MSCI Emerging Markets Total Return Index
BP	**Balanced Portfolio** 40% FTSE TMX Canada Universe Bond Index 40% MSCI World Index 20% S&P/TSX Composite Total Return Index

Investing Strategy		Ending Value	Annual Return	Standard Deviation
Chasing returns:	Always invest in the prior year's **top** performing asset class	217,352	8.07	12.74
Contrarian view:	Always invest in the prior year's **worst** performing asset class	210,402	7.72	8.71
Diversified:	Invest in 60/40 Balanced Portfolio* (rebalanced annually)	222,070	8.31	5.44

A Balanced Portfolio provides more consistent returns with less risk than consistently chasing the best/worst asset classes.

Source: Morningstar Direct, in Canadian dollars, as at December 31, 2020 for a 10-year period. Past Performance is not indicative of future results.

*60/40 Balanced Portfolio consists of 40% FTSE TMX Canada Universe Bond, 40% MSCI World C$, 20% S&P/TSX Composite TR

Historically, it is difficult to predict next year's top performing asset class.

- A key element in helping to achieve your financial goals is strategic asset allocation, which means establishing a mix of equities, fixed income and cash that is best suited to your risk tolerance and investment objectives, and holding this mix consistently.
- Take the guesswork out of trying to always pick the winners by diversifying your portfolio to capitalize on future changes in the market and the performance of each asset class.

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The chart above illustrates that it is difficult for investors to predict the performance of a particular asset class from year-to-year.

A strong tactical asset manager can help ensure that you have exposure to the best performing asset class in any given year

Do-it-yourself (DIY) investors typically invest in a basket of stocks, based on market research, help from a friend, or the latest hot tip from their favourite "Top 10 Investment Tip" blog. While their portfolios may appear to be diversified at first glance, they can lack important exposures by:

Asset class – the right mix of fixed income and equities is critical to reaching your financial goals

Geography – A global approach to investing will add more diversification to your portfolios and may lower market volatility

Sectors – ensure you have both cyclical and defensive sectors in your portfolio

Asset Allocation Investing

Asset allocation is one of the most important investment decision an investor will make in their portfolio. The asset allocation of a portfolio will determine how much to allocate to fixed income, equity and to cash:

- **Fixed Income –** Provides security and income
- **Equity –** Provides long-term growth and inflation protection
- **Cash –** Safety, liquidity

Fixed income, equity and cash all offer different characteristics, and each asset class reacts differently to market movements and to economic events. In this way, asset classes work together to bring an investor the right mix of risk, return, security and growth while maintaining a diversified portfolio.

Why Does The Mix Matter?

A portfolio's asset allocation will have the largest impact on an investor's long-term returns, more so than individual stock selection.

The decision between a conservative, balanced and growth portfolio reflects an investor's risk/return profile. An investor must define their return objectives and determine their ability and willingness to accept market risk. An investor must consider factors such as time horizon and investment goals. A longer investing time horizon allows for more allocation to riskier assets such as equities, this is because an investor has more time to recover from short-term corrections. Each investing goal has its own unique asset allocation. Saving for a house, retirement or for education would each have its own optimal asset mix.

> *"Asset allocation explains over 90 per cent of the variation in a portfolio's quarterly returns"*

1986 study by Brinson, Hood, and Beebower, "Determinants of Portfolio Performance"

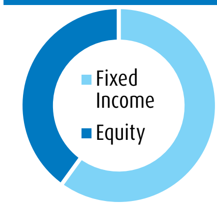
8 Reasons to Buy Asset Allocation ETFs

1. **Simplified Investing –** All-in-one Investment Solution that provides instant diversification
2. **Broad diversification –** Consisting of a basket of ETF that in themselves hold many securities
3. **Professionally constructed –** Leverage the Asset Allocation experience of industry professionals
4. **Automatic Rebalancing –** Keeps one's investment portfolio on track to risk and return objectives
5. **Transparency –** Knowing what is in the ETF can help reduce duplication when complementing a portfolio
6. **Liquid –** able to buy or sell the basket of holdings at any time
7. **Lower cost –** ETF based solutions tend to charge lower fees than other diversified investments
8. **All-in-one cost structure –** Most popular Asset Allocation ETFs only charge the one top fee without charging the underlying ETF costs

Continued

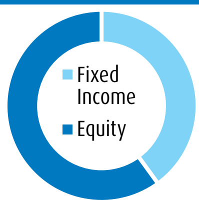
Examples of Asset Allocation ETFs in Canada

Conservative Asset Allocation ETFs



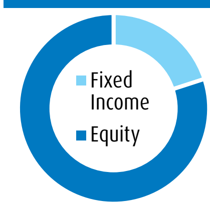
Name	Ticker	MER
BMO Conservative ETF	ZCON	0.20%
Vanguard Conservative ETF Portfolio	VCNS	0.24%
iShares Core Conservative Balanced ETF Portfolio	XCNS	0.20%

Balanced Asset Allocation ETFs



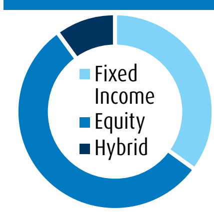
Name	Ticker	MER
BMO Balanced ETF	ZBAL	0.20%
Vanguard Balanced ETF Portfolio	VBAL	0.24%
iShares Core Balanced ETF Portfolio	XBAL	0.20%

Growth Asset Allocation ETFs



Name	Ticker	MER
BMO Growth ETF	ZGRO	0.20%
Vanguard Growth ETF Portfolio	VGRO	0.24%
iShares Core Growth ETF Portfolio	XGRO	0.20%

Monthly Income Asset Allocation ETFs



Name	Ticker	MER
BMO Monthly Income ETF	ZMI	0.20%

ESG Asset Allocation ETFs

Name	Ticker	MER
BMO Balanced ESG ETF	ZESG	0.20%

The portfolio holdings are subject to change without notice and only represent a small percentage of portfolio holdings. They are not recommendations to buy or sell any particular security.

BMO Global Asset Management