Views from the Desk

Updates in the Equity and Fixed Income Market

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China's Evergrande Effects on the Market

Evergrande is China's second biggest real-estate developer with 300 Billion in liabilities and is currently having some debt troubles. There are concerns of Evergrande being overleveraged and recently they missed a coupon payment of over $70 million dollars. The are concerns that further defaults could lead to more sell offs in the high yield credit market.

Many analysts are making comparisons to what happened to the Lehman Brothers during the financial crisis. We do think its China's best interest to intervene and it appear that they have been doing just that. Yesterday China gave another 20 billion to the Chinese banks to shore up Evergrande's missed coupon payment. Most of Evergrande's exposure is within the Chinese banking system. Within North America, the US banks have minimal exposure to Evergrande, and the Canadian banks have little to no exposure as well.

Regarding Evergrande and REITs. The market reaction is a great barometer of what investors are thinking. REITs were down a little more than the broad market on Monday. Canadian REITs had more of a reaction than global REITS however, Canadian REITs bounced back from Mondays sell off. ZRE - BMO Equal Weight REITs Index ETF

Bond yields

The markets have been relatively muted so far this week with fixed income. Spreads widened out a little bit but, has since come back. We expect increased volatility in the equity markets throughout the rest of the year, and we think it is important to have fixed income in your portfolio. ZAG - BMO Aggregate Bond Index ETF is an excellent way to get exposure across the yield curve and a smart way to get access to long exposure. Over the long term we believe that a balanced exposure across the curve is important as it takes the guessing out of where you want to be.

The Bank of Canada has been very prudent with their elimination and tapering of their bond buying programs. Furthermore, the Bank of Canada has been very successful at reducing Quantitative Easing (QE) without really impacting markets in a material way. We expect this to continue and the Bank of Canada to begin reinvesting in their bond purchasing programs again. Inflation did surprise us in August however, we believe it is still transitory and from a rate perspective, mid 2022 seems to be the forecast consensus to raise rates.

The Fed will comment later today, and we don't expect much to change and we expect the Fed to keep messaging relatively the same. We expect a soft tone from the Fed to keep volatility low in the markets. The Fed (like the Bank of Canada) is also looking at the second half of 2022 before they start raising rates. Lastly, we anticipate tapering to start later in 2021 (in the US).

Low Volatility

Being invested in equities that are less cyclical can be beneficial to your portfolio. ZLB - BMO Low Volatility Canadian Equity ETF is a great too to have in your portfolio when we see volatility pick up and the broader markets become volatile. ZLB is up 18% year to date matching ZCN - BMO S&P/TSX Capped Composite Index ETF.

The performance of Shopify last year affected ZLB since we did not have it in the low vol portfolio. Shopify has started to moderate this year which has helped out ZLB. The Canadian Low volatility ETF is managing risk as expected and is designed to avoid highly cyclical sectors in hopes to bring alpha to your portfolio.

Canadian Election

The 2021 Canadian election results ended up very much the same as the results in 2019. This minority government has been effective over the last 2 years to get things done and we view this as a positive going forward. In terms of policy, we see 2 themes that can emerge from an investment perspective. The Liberals have been ambitious around Clean Energy and have a goal to reach “net zero emissions” by 2030 and $170.00/tonne carbon tax by 2050. We do think the trend is clear across the spectrum and echoed across the globe to reduce carbon emissions overall. ZCLN - BMO Clean Energy Index ETF is going to be topical over the next several decades and the adoption of clean energy is only going to increase.

The second theme that we want to identify is inflation fears. The Liberals (with the support of the NDP) are expected to increase fiscal stimulus across the board which could bring inflation pressure. Fiscal spending could lead to the dilemma of inflation vs raising rates. To protect yourself against Canadian inflation we look at ZRR - BMO Real Return Bond Index ETF. For more on the Canadian election please visit The Canadian Election Aftermath - As We Move On.

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Source: Bloomberg, All returns and data points September, 2021.
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