March 24, 2020

Canadian Strategy Snapshot

COVID-19 Positioning and the Expected Canadian Recovery

Three Rational Canadian Scenarios to Cope With the Irrational and Unknown

The coronavirus (COVID-19 virus) crisis and the adjacent fear generated by its human tragedy have produced collateral economic and societal anxiety that is unprecedented to say the least. Furthermore, there is no denying the collapse of oil prices and the indefinite shutdown of the global economy have positioned Canadian economic and stock market forecasts with nearly impossible levels of uncertainty. As such, we believe traditional fundamental forecasting methods including, but not limited to, dividend discount, valuation reversion, and economic regression models are likely to be poor guideposts over the near term. Therefore, we believe it is prudent to suspend our CY2020 S&P/TSX price and earnings targets and shift to a rolling 12-month forward model. As markets become more rational, we believe the efficacy of point-in-time forecasts will follow suit. This malaise and anxiety will dissipate. When it does, there is no reason to believe that Canadian stocks will not return to fundamentals and see similar daily upside moves relative to the exacerbated weakness of the past few weeks.

Main Points:

- Three Scenarios for Canadian Stocks
  1) COVID-19 Case: Next 1-3 months – Defense and COVID-19-centric Themes
  2) Base Case: Next 12-18 months – Rebound and Canada's Role in the Recovery
  3) Secular Case: Next 3-5 Years – Early Stages of Global Re-synchronization

- Transitioning Targets to 12-month Rolling – Staying the course and NOT panicking
  - S&P/TSX Price Target: 18,200; EPS: $1,020
  - Suspending CY2020 S&P/TSX Price and Earnings Targets
  - CY2020 targets will carry more merit in our view once the bottom and recovery take shape

BMO Capital Markets

Investment Strategy

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Major Indices Price % Performance

Index	1M	YTD	6M	12M
S&P/TSX	-29.5	-26.3	-25.6	-21.8
S&P/TSX 60	-27.3	-23.9	-23.6	-19.2
S&P/TSX Small Cap*	-46.0	-46.3	-45.7	-45.5
S&P 500	-26.7	-24.2	-18.2	-12.5
DJ Industrial Average	-28.6	-27.4	-23.1	-18.9
NASDAQ Composite	-22.5	-17.3	-8.6	-2.9
MSCI EAFE*	-30.1	-29.2	-26.2	-22.9
MSCI Emerging Mkt*	-26.8	-27.3	-22.0	-22.5
MSCI EMEA*	-30.2	-31.4	-29.3	-28.1
MSCI Europe*	-32.2	-30.9	-28.0	-24.2

Source: BMO Capital Markets Investment Strategy, FactSet.
Performance figures reflect close prices as of 3/24/2020
* Performance reflect close prices 3/23/2020

18:21 ET | 18:21 ET

COVID-19 Positioning and Canada's Role in the Recovery

COVID-19 Case – Time Frame: Next 1-3 Months

Bottom Line: The Virus That Killed the Bull Market & Suspending Our CY2020 S&P/TSX Targets

The coronavirus (COVID-19 virus) crisis and the adjacent fear generated by its human tragedy have generated collateral economic and societal anxiety that is unprecedented to say the least. Furthermore, there is no denying the collapse of oil prices and the indefinite shutdown of the global economy have positioned Canadian economic and stock market forecasts with nearly impossible levels of uncertainty. As such, we believe traditional fundamental forecasting methods including, but not limited to, dividend discount, valuation reversion, and economic regression models are likely to be poor guideposts over the near term. Therefore, we believe it is prudent to suspend our CY2020 S&P/TSX price and earnings targets and shift to a rolling 12-month forward model. As markets become more rational, we believe the efficacy of point-in-time forecasts will follow suit. This malaise and anxiety will dissipate. When it does, there is no reason to believe that Canadian stocks will not return to fundamentals and see similar daily upside moves relative to the exacerbated weakness of the past few weeks. Therefore, our new rolling targets will provide us with flexibility to adjust as necessary during these fast-moving markets while also providing timely insight as it relates to our market outlook. With that being said, we are maintaining our previous levels for both forecasts – 18,200 for price and $1,020 for EPS for the next 12 months.

Strategy: Defense & COVID-19 Theme Related

- Given the concentrated nature of the Canadian stock market, our more defensive and COVID-19-related strategy is generally sector agnostic.
- Preferred positioning should be a mix of defense (Staples, REITs, and Utilities), and COVID19-related topical themes (Communication Services and Technology).

Nineteen Coronavirus (COVID-19) Themed Stocks for Canadian Investors

Ticker	Company	Price	Rating
AEM	Agnico Eagle Mines Limited	64.23	OP
AQN	Algonquin Power & Utilities Corp.	15.24	OP
ATD.B	Alimentation Couche-Tard Inc. Class B	34.2	OP
BCE	BCE Inc.	50.85	OP
BIP.UN	Brookfield Infrastructure Partners L.P.	47	OP
CP	Canadian Pacific Railway Limited	299.55	OP
CTC.A	Canadian Tire Corporation, Limited Class A	83.8	Mkt
DOL	Dollarama Inc.	37.87	Mkt
ENB	Enbridge Inc.	39.37	OP
HR.UN	H&R Real Estate Investment Trust	8.16	OP
L	Loblaw Companies Limited	63.64	OP
RCI.B	Rogers Communications Inc. Class B	52.75	OP
REI.UN	RioCan Real Estate Investment Trust	14.7	OP
RY	Royal Bank of Canada	81.75	Mkt
SAP	Saputo Inc.	33.36	Mkt
SHOP	Shopify, Inc. Class A	628.4	NR
T	TELUS Corporation	20.48	Mkt
TD	Toronto-Dominion Bank	55.89	Mkt
WCN	Waste Connections, Inc.	109.34	OP

Source: Factset, BMO Investment Strategy Group

Investment Strategy Base Case – Time Frame: Next 12 Months

Bottom Line: Prepare for the Recovery – Because It Is Coming With a Vengeance

Traditionally, Canadian equities tend to exhibit a "delayed effect" during sharp corrections and/or bear markets with respect to their relative performance to the U.S. Not this time around. In fact, the TSX has mostly been following lock step with the SPX as the COVID-19 crisis has accelerated. We believe this not only accentuates Canada's fundamental relationship with the U.S., but also speaks to the emotional and excessive anxiety-laden investment atmosphere. However, this too shall pass, and when it does, there is no reason to believe that Canadian stocks will not follow their U.S. neighbour to the south and see similar daily upside moves relative to the exacerbating weakness of the past few weeks. While unprecedented monetary and fiscal policy is unlikely to secure the market's bottom, there is no denying the massive fuel that both will provide the eventual recovery. As such, we remain optimistic over the longer term and believe Canadian equities are likely to follow the U.S. blueprint, particularly those companies levered to U.S. growth (as America goes, so goes Canada). Admittedly, the pushback to own Canadian stocks is loud and clear while polling consensus = "Canada is not open for business." We beg to differ. As such, we stand behind our 12-month price target of 18,200 on earnings of $1,020.

Strategy: Canada = A Backdoor Value Proposition to Own the U.S.

- We continue to believe the strength and stability of current and future cash flow and earnings power will come from companies whose primary or incremental growth is coming from or geared toward the U.S.
- While a cyclical rebound will likely be powerful, quality measures such as operating performance and earnings stability should be a primary area of focus within areas like Industrials, Energy, and Materials.
- Lower interest rates will undoubtedly help REITs and Utilities, while forcing positions within Financials to be more concentrated (within the big players). As a result, we are neutralizing our positioning within Utilities to Market Weight from Underweight.
- Energy Overweight? Yes. We are an embargo or V-shaped recovery away from a massive rally. Furthermore, our preferred positions employ very concentrated and high-tracking error positioning to pipes and integrated oil (yield and cash flow).
- Neutralizing position in Utilities (from Underweight) due to excessively low interest rates.

Sector	Opinion	%Weight	Theme
Communication Services	OW	7.5%	Yield, content and cash flow; work from home is a major positive
Consumer Discretionary	MW	3.5%	Staples-oriented retail and lifestyle
Consumer Staples	MW	5%	Discretionary retail
Energy	OW	13%	Focus on yield and cash flow only; languishing underlying commodity likely to persist
Financials	OW	31%	Multi-divisional; biggest of the big – especially those focused on the U.S. – are best positioned
Health Care	UW	0%	Prefer U.S.
Industrials	MW	12%	Will benefit from a cyclical recovery, but stick with high quality
Information Technology	MW	7.5%	On-line shopping has become a necessity; wireless and broadband budgets to explode
Materials	MW	13%	Stay diversified; rebound for metals is coming, but focus on quality
Real Estate	OW	3.5%	Yield and cash flow; lower-for-longer interest rates to provide support
Utilities	MW	5%	Yield and stability of dividend; lower-for-longer interest rates to provide support

Source: BMO Investment Strategy Group

Investment Strategy Secular Case – Time Frame: 3-5 Years

Bottom Line: Still Waiting for Early Stages of Global Re-synchronization

Canada's surprise stock market performance in 2019 – especially relative to other developed markets (ex-U.S.) awakened many investors to Canada for the first time in several years, based on our client interactions. Unfortunately, COVID-19, the oil shock, and a nasty bear market have caused a reset in Canada – not unlike other developed markets. As the recovery unfolds, we continue to believe it will follow alongside the U.S. – perhaps not to the same magnitude, but at least attempt to mirror the U.S. nonetheless. The $64,000 question is when will Canada once again enjoy the spoils of global synchronized growth? That remains to be seen in our view. Undoubtedly, resources and energy will have their heyday again – as early as within the next 3-5 years – and yes – Canada will be among the leaders with respect to developed market equites – even outpacing the U.S. at some point. In the meantime, investors should take solace in the fact that Financials are in the best credit and balance sheet condition in several generations. Another major positive in our view is the increased diversification within the index. Yes, the Big 3 sectors (Financials, Energy, and Materials) receive much of the limelight and scorn. However, the growing importance of Communication Services and Technology are bearing fruit – especially when examining the Technology sector weight within the TSX. While naysayers would say that the index weighting within Technology is primarily one stock – and yes – we have seen that party before in Canada – the interrelation of Communication Services, Technology, and even Consumer Discretionary cannot be discounted. Be patient – oil and gold will come back. In the meantime, enjoy those companies levered to U.S. growth and prepare for global markets and commodities to regain their footing.

Select Themes/Subjects to Consider Heading Into the Next 3-5 Years

Theme/Subject	By-product Question
The Mobile Worker	Broadband and wireless capacity? New technology and communications equipment?
Social Distancing	Do office spaces change back from open concepts to offices again? What happens to restaurant spacing and service providers? New regulations?
Energy	Acceptance of the Range, Cost Management, M&A?
U.S. Secular Growth	Cross-border M&A or renewed innovation in Canada (especially Technology)
Re-Thinking Supply Chains	Railroads; increased domestic production?
Buybacks and Dividends	Low interest rates have historically fueled both dividends and buybacks. But will shareholder and public fallouts force legislation against buybacks?

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Buy	Outperform	44.3 %	26.2 %	53.9 %	45.6 %	54.5 %	57.7%
Hold	Market Perform	52.0 %	18.0 %	43.5 %	51.1 %	44.4 %	37.5%
Sell	Underperform	3.7 %	15.0 %	2.6 %	3.1 %	1.1 %	4.8%

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

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