BMO's "Five Lenses" Strategy

BMO Multi-Asset Solutions Team

At BMO Global Asset Management (BMO GAM) we recognize that asset allocation is the primary driver of long-term portfolio performance. That's why we've created a group of asset allocators called the Multi-Asset Solutions Team (MAST), who follow a consistent investment philosophy to focus on global idea generation with local portfolio implementation. The MAST has developed a simplified "Five Lenses" view to help explain what is driving their asset allocation decisions.

Lens 1

Asset Mix

- Equities
- Fixed Income
- Cash

Lens 2

Asset Class - Equity

- Regional Equities
  - Canada
  - U.S.A.
  - EAFE
  - Emerging Markets
- Alternative Investments

Lens 3

Asset Class – Fixed Income

- Duration
- Investment Grade Credit
- High Yield
- Emerging Market Debt
- Alternative Investments

Lens 4

Style/Factor

- Value
- Momentum
- Volatility
- Growth
- Quality
- Size
- Yield

Lens 5

Implementation

- Active vs. Passive
- Derivatives
- Currency Selection

At BMO GAM, we've always promoted the value of long-term investing. To us, that's always been the most important decision. In a similar vein, the Five Lens process begins with the strategic asset allocation, which takes into account the long term expected returns, standard deviations and correlations of various asset classes, adjusted for recent experience. This establishes our longer-term view (4-5 years) that defines the neutral asset mix and the design choices of each portfolio (subject to its objectives). However, we recognize that there are times when our short term views (3-12 months) differ substantially from our longer term views. This is where our tactical asset allocation is employed, and forms part of our risk management framework. How we make our tactical asset allocation decisions forms the DNA for our Five Lenses. Our process first decides where we want to be more or less bullish, whether we need to adjust our geographic weightings (both within equities and bonds) and whether there are certain exposure we like to have more or less of (i.e., high yield vs. corporate bonds). We then decide whether there are certain styles or factors we want to adjust. The process concludes with how we want to implement those changes. We update tactical changes via our scorecard and communicate it via the Fives Lenses each month. Each portfolio is designed with specific portfolio parameters in mind to allow for sufficient degrees of freedom to implement meaningful tactical calls when appropriate, such as overweight U.S. equities, for example. For us, portfolio management involves both strategic and tactical decisions. We will continue to evolve our Five Lenses Strategy to produce better outcomes for our clients.

Five Lenses, as of December 2022

Lens 1
Asset Mix

- Aggressive monetary-policy tightening is increasing the odds of global recession, but the odds of a soft landing have recently increased as the U.S. economy proved more resilient than feared.
- Bonds could soon be attractive once the recession starts.
- Now neutral across equities and bonds, but the lingering uncertainty around the economic outlook should bring choppy markets over coming months.

Tactical Score:

Equities	0
Fixed Income	0
Cash	0

Lens 2
Asset Class - Equity

- Downgraded North American equities to neutral as economic growth slowed due to rate hikes.
- Europe remains challenged by the energy outlook, but the severity of the energy shock, while severe, appears more manageable than expected.
- China is set to continue lifting COVID-related restrictions, which should provide a significant tailwind to its economy and support the broader EM complex.

Tactical Score:

Canada	0
U.S.A.	0
EAFE	-1
EM	+1

Lens 3
Asset Class - Fixed Income

- Rates hikes are not done, but we are nearing the peak of the hiking cycle while the pace of economic growth is moderating.
- Inflation remains elevated and a concern for markets, but we expect markets to increasingly worry about an economic slowdown.
- We think riskier high-yield credit is exposed to a worsening economic outlook.

Tactical Score:

IG Credit	+1
High Yield	-1
EM Debt	0
Duration	0

Lens 4
Style/Factor

- Value stocks are well positioned for sticky inflation and energy cycle.
- Growth stocks could suffer in the early innings of the recession because of their higher multiples.
- Quality and low volatility companies should be well shielded against economic and earnings downside.

Tactical Score:

Value	+1
Quality	+1
Growth	-1
Volatility	-1

Lens 5
Implementation

- As we approach the end of the U.S. Federal Reserve hiking cycle, we expect to see a broad decline of the U.S. Dollar, which should benefit the Canadian dollar into 2023.
- The rising odds of U.S. soft landing should also alleviate demand for safe-haven U.S. assets.

Tactical Score:

CAD	+1

-3	-2	-1	0	+1	+2	+3
Very Bearish	Bearish	Slightly Bearish	Neutral	Slightly Bullish	Bullish	Very Bullish
<-5.0%	-5.0 to -2.5%	-2.5 to -1.0%	-1.0 to +1.0%	+1.0 to +2.5%	+2.5% to +5.0%	>+5.0%