

2025 Capital Markets Outlook

Bunches and Punches

Brent Joyce, CFA

Chief Investment Strategist

BMO Private Investment Counsel Inc.

All data references are as of November 15, 2024 unless otherwise stated.

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Executive summary

In last December's 2024 Market Outlook [Plenty of Progress, Solid Foundations Laid](#), we discussed a continuing return to normal, an environment where investors are rewarded across the risk spectrum. After a decade of absence, normal – or normal uncertainty – has finally returned.

We see the fundamentals of economic growth, corporate earnings, inflation, bond yields and sentiment as supportive. Valuations are a mild hurdle in some markets, attractive in a few. We think valuations are manageable in U.S. markets. We see a path to further (modest) gains, but we could at any time face a growth scare, which is a normal, minor correction that occurs in bull markets.

Headwinds are abating: specifically, slow economic growth, lacklustre corporate earnings growth, high inflation, elevated interest rates and bond yields, sluggish lending, and weak consumer and business sentiment. Some tailwinds are blowing in. Markets deliver returns in waves or bunches. Inevitably, a series of strong returns is followed by punches, or pullbacks, that trim the excesses in markets through corrections and bear markets or sideways movements.

Globally, there is a powerful alignment of falling inflation and smooth-sailing economies (U.S.) and economies that are doing okay (Canada, the U.K. and most of Europe).

Equity markets

The positive global macroeconomic backdrop points to solid corporate earnings growth expectations for 2025, ranging from 9% to 15% globally.

We believe it's more likely we'll get positive earnings surprises than the opposite.

Equity market valuations (12-month forward price-to-earnings ratios) diverge across our four major markets. Valuations are above normal in some markets. Earnings growth in the teens, even on extended valuations, can deliver high-single to low-double-digit market returns. With high earnings growth and continued elevated valuations, another year of exceptional equity market returns is possible.

We are overweight equities. We believe equities can deliver mid-teens total returns. Our targets are 28,600 for the S&P/TSX Composite and 6,600 for the S&P 500.

Fixed income markets

We expect the Bank of Canada to drop the overnight rate from 3.75% to 2.5% by June 2025 and then hold. We expect the U.S. Federal Reserve to lower the fed funds rate from 4.75% to 3.5% by the end of 2025.

Canadian 2-year and 10-year bond yields are at 3.15% and 3.28%. For the U.S., yields are 4.31% and 4.44%. We think yields will fall as central banks lower benchmark rates.

Our end-of-2025 call is for the yield curve to steepen, with Canadian 2-year bond yields of 2.75% and 10-year bond yields at 3%. This should drive total return in the broad Canadian fixed income market in the 4% range.

Currency outlook

We don't see the loonie's fortunes turning around imminently, but given the extent of the pessimistic sentiment, we believe most of the weakness is done.

We expect the loonie to appreciate, with an exchange rate of C\$1.35 or US\$0.74 at the end of 2025.

Our positioning

Our portfolios remain well diversified and balanced, favouring equities over fixed income.

In our broadest representative portfolios, **we are overweight Canadian and U.S. equities**, neutral to international developed markets (Europe and Japan) and underweight emerging markets.

We are overweight investment-grade corporate bonds and underweight the lowest-quality borrowers in high yield.

The current yield from our well-diversified bond positions is very competitive.

The last word

We remain constructive on the investment outlook for 2025.

We conclude that the fundamentals of economic growth, corporate earnings, inflation, bond yields and sentiment remain supportive. Valuations are mixed. Therefore, we continue to rely on diversification across geographies and asset classes – stocks, bonds, cash, and alternatives – to meet our clients' individual investing objectives.

Overview

For more than two years, our views on capital markets have been heavily influenced by global economic reverberations and fallout from the pandemic. In last December's 2024 Market Outlook [Plenty of Progress, Solid Foundations Laid](#), we discussed a continuing return to normal. We can now say that normal – or more accurately normal uncertainty – has finally returned.

Our process when forecasting asset-class returns begins with an examination of long-run averages. We then scan for reasons why there could be a deviation. We are also highly attuned to the fact that capital markets don't always deliver long-run return outcomes in neat and tidy packets of monthly or annual returns that are close to the average. They regularly overshoot and undershoot what the fundamentals justify. Markets deliver returns in waves or bunches. Inevitably, a series of strong returns is followed by punches, or pullbacks. These punches alleviate the excesses in markets through corrections and bear markets or sideways movements that allow fundamentals to catch up to prices.

Looking ahead to 2025, our forecasts for cash, bonds and alternatives call for reasonably normal returns in line with their long-run averages. For equity markets, we see the potential for the current string of above-average returns to continue. At two years and counting, we are not yet at a bunch. The upside opportunity for equity markets is based on the potential for above-average global economic growth and inflation.

While this is not our base case scenario, if stock markets are squaring up to land a punch, we believe that the damage would be in the normal historical range for non-crisis bear markets. The last 25 years witnessed two of the worst bear markets in the last 100 years (S&P 500 dotcom bust -49%, and financial crisis – 56%), which has conditioned investors to think these routs are the norm. Non-crisis bear markets are downdrafts of -20% to -25%, lasting no more than two or three quarters. If this scenario does unfold, we see a high probability that the bond market, unlike the situation in 2022, is set up to deliver downside protection to portfolios.

Cash is no longer king. Nevertheless, it remains a useful tool. Alternative investments (real estate, infrastructure, hedge funds, private equity and private credit) continue to play an increasingly important role as solid return generators and good diversifiers to stocks, bonds and cash.

We see the fundamentals of economic growth, corporate earnings, inflation, bond yields and sentiment as supportive. Valuations are a mild hurdle in some markets, attractive in a few. We believe with a deft touch applied, valuations are manageable in U.S. markets. We see a path to further gains, albeit more modest ones. Bull markets do come with interruptions called growth scares, where a few bad economic data points call the health of the global economy into question. They are to be expected and are typically run-of-the-mill -5% to -15% corrections. Stay calm and carry on; these are the uncertainties that present opportunity.

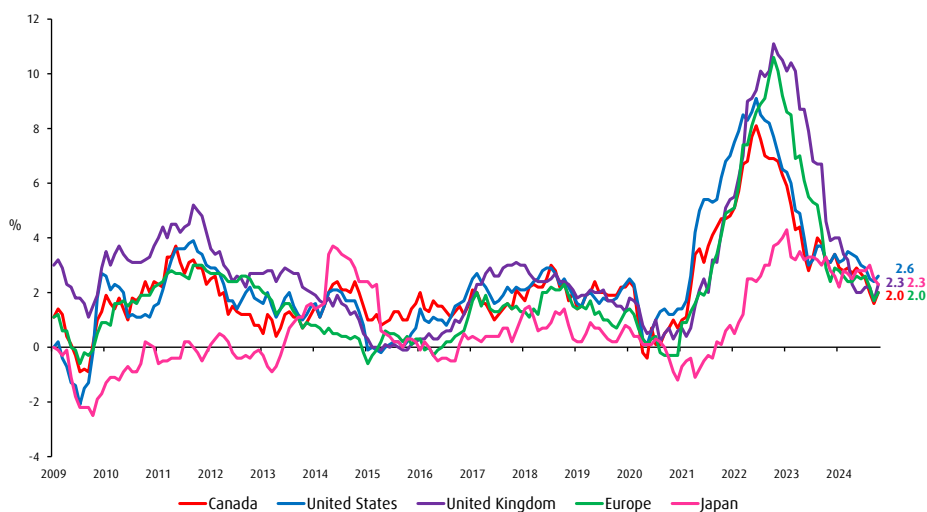
Macroeconomic backdrop

Inflation’s surge was the linchpin of the pandemic disruptions. It spurred central banks to tighten their monetary policy with a vice-like grip that hadn’t been seen in decades. Inflation is beaten or on the run (for now). While there is still a lingering sting in the tail from inflation and monetary policy tightening, central bankers are now heading toward normalizing interest rates.

(See Exhibit 1: Inflation on the Run and Exhibit 2: Central Banks – About Face)

Exhibit 1: Inflation on the Run

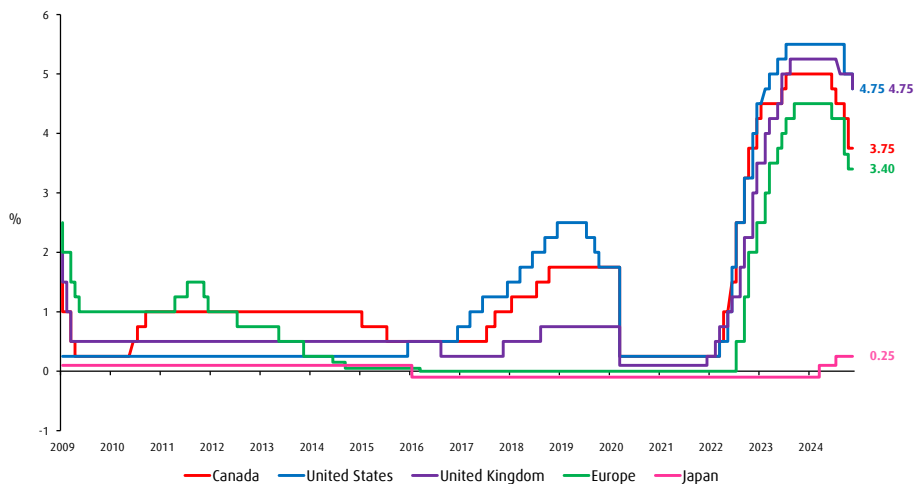
Year-over-Year Change in CPI for Selected Global Economies
January 2009 – October 2024



Source: Bloomberg

Exhibit 2: Central Banks – About Face

Central Bank Policy Rates of Selected Global Economies
January 1, 2009 – November 15, 2024



Source: Bloomberg

Throughout the past two years, the “how high for how long” conversation dominated while inflation was hot and central banks were tightening. Today, the question has shifted: “Where will interest rates land and when will they get there?” **We are still at the stage of falling policy rates, which is positive for capital markets.** Based on local conditions, the timing and magnitude of rate cuts vary among central banks. The overall trend will be lower rates in 2025 (Japan is set to raise rates some, but is starting from ultra-low levels).

The monetary tightening cycles had a negative impact on global economic growth during the years of high interest rates and concerted inflation-fighting. By design, tight monetary policy reined in the supply and demand for credit: banks were less willing to lend, and businesses and consumers were less willing to borrow. Interest-rate-sensitive housing and manufacturing sectors slowed, as did broader economic growth in those countries with greater sensitivity to interest rates (just about everyone except the U.S.).

Inflation has been wrestled to submission in many economies. It has yet to tap out in the U.S. but is on the ropes. Consumer and business sentiment, long moribund under the weight of these negatives, is beginning to perk up and embrace the idea that it is time to move on.

These headwinds – slow economic growth, lacklustre corporate earnings growth, high inflation, elevated interest rates and bond yields, sluggish lending, and weak consumer and business sentiment – are abating. In their wake, some tailwinds are blowing in.

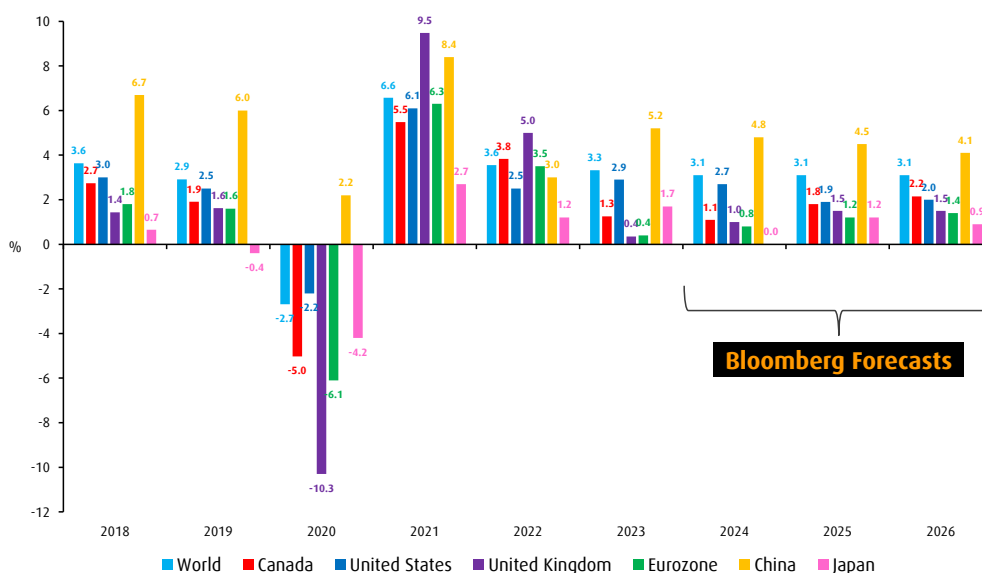
Most countries are getting inflation under control, with 70% of OECD countries now boasting annualized inflation below 3%. In fact, there are pockets where inflation is too low for comfort: in one-third of OECD countries inflation is below 2%. This is the key to allowing central banks to continue easing monetary policy, setting in motion a thaw in bank lending and creating conditions where bond yields can ease further. This will release pent-up activity in the housing and manufacturing sectors, ease consumer finances, and bolster economic growth.

Globally, there is a powerful alignment of falling inflation and smooth-sailing economies (U.S.) or economies that are holding up better than feared (Canada, the U.K., and a good chunk of Europe).

Germany’s economy is sluggish, but government finances are among the world’s strongest. China’s economy has slowed to the point where authorities have ditched the piecemeal approach to resuscitation. They are turning to more significant economic stimulus measures, including targeting the real estate sector, equity markets, and lower-income households. **(See Exhibit 3: Decent Economic Growth Expected)**

Exhibit 3: Decent Economic Growth Expected

Actual and Forecasted Year-over-Year GDP Growth Rates of Selected Global Economies
Actual: 2018 – 2023; Forecasts: 2024 – 2026 (as of November 15, 2024)



Source: Bloomberg

Sentiment also ebbs and flows with the bunches and punches of capital markets. While we aren't relying on further expansion of equity market valuations to arrive at our equity market forecasts, we note that there is plenty of historical precedent for market enthusiasm to get carried away. Broadly, we don't think this is the case yet. However, if this scenario does unfold, equity markets will rack up another exceptionally good year in 2025. We are comfortable being overweight equities on the fundamentals alone, but if the tide flows this way then the preferred positioning is overweight equities.

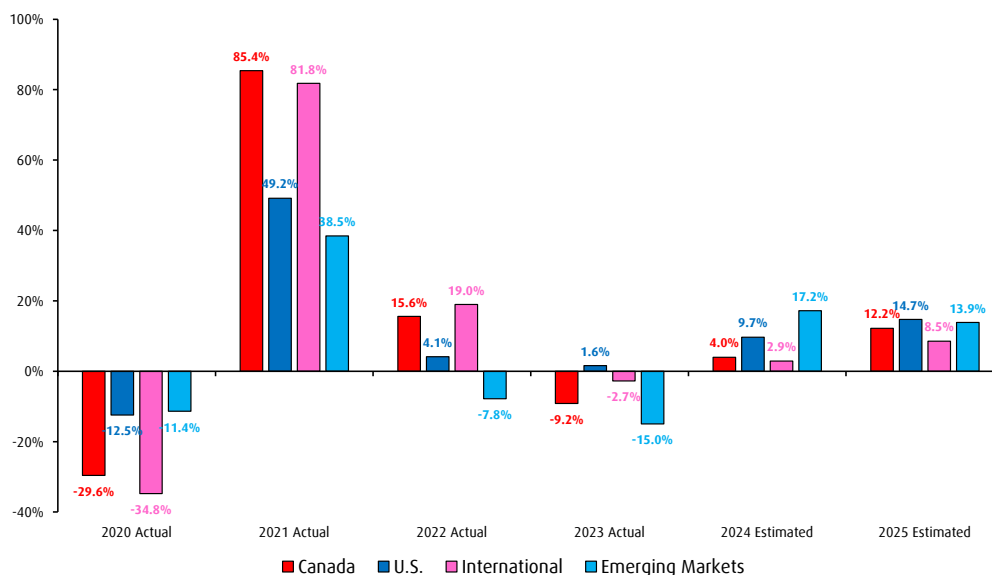
Capital Market implications – Equity markets

The positive global macroeconomic backdrop points to solid corporate profit growth. Corporate earnings and profit growth are the lifeblood of share price advances.

Corporate earnings growth expectations for 2025 range from 9% to 15% globally. **(See Exhibit 4: Global Earnings Growth Expectations)** Equity market valuations (specifically 12-month forward price-to-earnings ratios) diverge across our four major markets. **(See Exhibit 5: Valuations Require a Deft Hand)**

Exhibit 4: Global Earnings Growth Expectations

Earnings per Share Growth Estimates for Selected Global Markets
as of November 15, 2024 / November 18, 2024 (Canada)

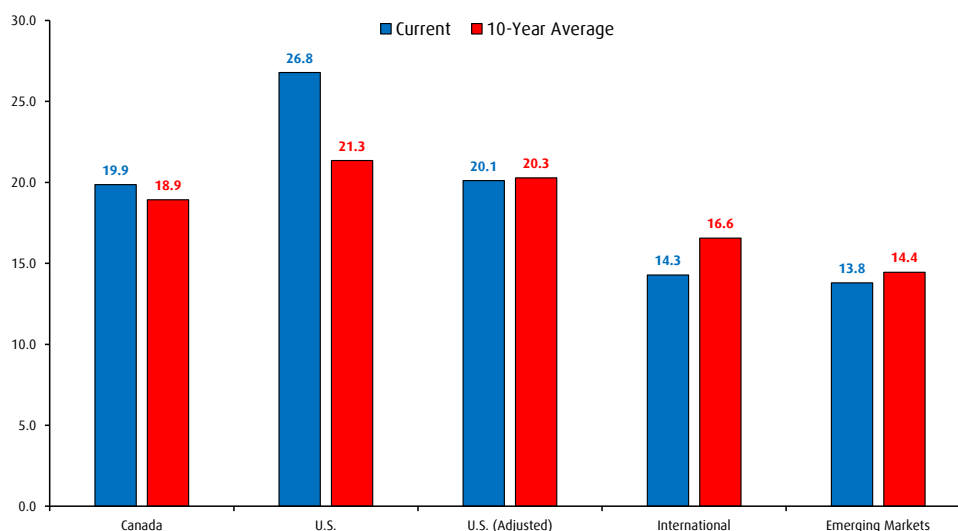


Source: FactSet

Canada: S&P/TSX Composite Index; U.S.: S&P 500 Index; International: STOXX Europe 600 Index; Emerging Markets: iShares MSCI Emerging Markets ETF

Exhibit 5: Valuations Require a Deft Hand

Current vs. 10-Year Average Price-to-Earnings Ratios of Selected Global Equity Markets as of November 15, 2024



Source: Bloomberg, trailing price-to-earnings ratio

Canada: S&P/TSX Composite Index; U.S.: S&P 500 Index; U.S. (Adjusted): S&P 500 Equal Weight Index; International: MSCI EAFE Index; Emerging Markets: MSCI Emerging Markets Index

Canada

The S&P/TSX Composite has enjoyed a solid rally during the back half of 2024. Former headwinds of the last several years are turning into tailwinds. These tailwinds are in sync with a renewed enthusiasm for Canadian equities, which have been out of the spotlight and unloved by domestic and foreign investors alike for much of the past decade-plus. The S&P/TSX is not the Canadian economy – our market is very globally oriented. Only a handful of companies have fortunes tied solely to the Canadian economy (e.g., grocers, telcos, utilities). The vast majority of S&P/TSX companies are globally oriented businesses, with the U.S. as our largest customer.

Our economy is projected to perk up. Most importantly, Canadian businesses should benefit from easier and cheaper financing, a weak currency, a solid U.S. economy, and a reacceleration in global economic activity. Our weak loonie is difficult for some but boosts exporters and inflates repatriated profits from Canadian companies' U.S. operations (e.g., banks and insurers).

Canada is benefitting from an \$8 billion U.S. trade surplus, largely in commodities (oil, metals) and motor vehicles. These commodities are of strategic importance to the U.S. and the vehicles are produced by U.S.-owned companies. Americans like cheap gas, so we don't see President-elect Donald Trump putting tariffs on oil. In the same vein, it would also be surprising to see tariffs on critical metals and uranium needed for a nuclear power renaissance. Tariffs conjure up images of steel, forest products, food stuffs and auto parts. These are important to the Canadian economy, but their weighting on the Canadian stock market is minimal. As a percentage weight of the companies that make up the S&P/TSX, steel is 0.1% (Algoma, Labrador Iron Ore), paper and forest products 0.4% (West Fraser, Stella-Jones), food products 0.3% (Saputo, Maple Leaf), and automobile components 0.5% (Linamar, Magna).

By way of comparison, metals and mining account for 10%, energy 18% and financials 33%.

Metals, mining, and energy should get a light touch (perhaps benefit) under the new administration. Plus, all the U.S. domiciled operations of any foreign business should not see any tariffs but would benefit from lower U.S. corporate taxes and deregulation. This includes Canadian bank branches in California, Chicago-land, the Carolinas, Florida and beyond (e.g., Royal Bank, TD and BMO). Canadian insurance giants SunLife, Manulife and Canada Life all have U.S. domiciled operations. These revenue streams would not be negatively impacted. Ditto for German, Korean and Japanese auto plants in the U.S. This is exactly the kind of thing Trump wants: "Hey, big successful global businesses, want to sell to America? Then build and operate in America." For many Canadian businesses, this is already the case. Oh, and don't forget Timmies outlets in the U.S., Popeyes, and Burger King – no tariffs either. All three brands are owned by a S&P/TSX-listed company.

Investors are taking notice of Canadian equities; inflows have picked up, and valuations have risen from slightly below to slightly above their longer-run average. Respectable valuations and a solid 3% estimated 2025 dividend yield make Canadian stocks attractive.

Europe, Asia, and the Far East (EAFE)

Valuations for developed markets in Europe, Asia and the Far East (EAFE) are below their longer-run average. However, Europe, the U.K., and Japan face various limiting structural problems, including relatively weaker economic growth, war and geopolitical instability, demographic concerns, and poor productivity, to name a few. They are cheaper for a reason. **Earnings growth expectations are modest at high single digits, but the estimated 2025 dividend yield is a healthy 3.4%.** Our three active equity managers in the EAFE arena have done an excellent job of extracting excess returns in these markets.

United States

For the U.S. market, a variety of crosscurrents are in play. U.S. equities are not cheap, but they also feature some of the best earnings growth expectations plus a host of positives and potential positives. Only a few caveats.

The U.S. government and the U.S. consumer were two outliers in the slow global growth of the last two years. Uncle Sam was seemingly immune to (more correctly oblivious to) higher borrowing costs. Meanwhile, U.S. consumption benefitted from the government's largesse, a surge of immigration, rising real wages, and homeowners insulated by legacy low mortgage rates under a unique U.S. mortgage system that features a 30-year fixed rate.

We see U.S. economic growth and elevated inflation set to continue, albeit with growth not as strong and inflation not as high. Consumer spending and business investment remain healthy. It's estimated that large fiscal spending initiatives have deployed just 30% of their funds. These initiatives are aimed at addressing infrastructure, energy, electricity demand, technology and green initiatives (IRA, Infrastructure, and CHIPS legislation). The incoming administration may look to curtail some of these initiatives. But if 70% of funds have yet to hit the economy, a fiscal boost is still going to flow even after reductions.

On top of this, we have the prospect of further grassroots stimulus. Some personal tax relief is possible (reinstating SALT deductions and tax-free tips), but at a minimum, tax increases aren't expected. Promises of corporate tax cuts are a positive for U.S. stocks. A quick calculation shows about a 5% bump to S&P 500 earnings per share if the corporate tax rate is lowered to 15% from 21% for companies that produce goods in the United States. That includes divisions of non-U.S. companies operating in the U.S. – think Canadian banks and insurers and Asian and European automakers, for example.

An added plus for U.S. businesses is the expectation of a lighter regulatory touch from the incoming Republican-controlled Senate, which is responsible for confirming the cabinet and regulators. This can flow directly to the bottom line through improved profit margins. Share prices reflect earnings growth, which is a function of revenues and profit margins. Solid economic growth leads to increased sales and revenue. Add that to fatter profit margins and earnings growth could see positive surprises in 2025.

Additionally, we have strong indications that the U.S. is enjoying a productivity boom. Productivity feeds all mouths – corporate earnings, worker wages and government revenues from taxes on both, all with little inflationary impact. Productivity drove spectacular stock market returns in the 1980s and 1990s. We've enjoyed two years of above-average returns, which is nowhere near the run of strong market returns that those earlier periods produced.

Many of these positive fundamentals are evident now, but some of the current wind beneath equity-market wings is fashioned from hopes and promises (tax cuts, solid spending by households, businesses and government). Negatives must also be considered: tariffs, possible trade wars, along with rising interest rates and inflation caused by government borrowing and spending.

Tariff-man Trump

President-elect Donald Trump fancies himself a dealmaker and has talked about tariffs as a negotiation tool. Tariffs under a Trump administration could range from surprisingly benign (simply a tool to strike deals) to the opposite end of the spectrum where trade wars and drawn-out, tit-for-tat retaliation create economic disruptions. His approach to America-first tariffs remains a significant source of uncertainty.

Most economists see tariffs as bad policy. But it's not a black and white situation. Some counterbalances would dampen the negative impact. While tariffs are a tax on the businesses and consumers in the country imposing them (Americans in this case), if no offsetting tax cuts are made then this does improve the U.S. fiscal picture. The strengthening U.S. dollar (on top of an already strong U.S. dollar) also somewhat offsets the downside because it softens the impact on exporters to the U.S. and dampens the inflationary impact inside the U.S. We are optimistic that the most egregious tariff proposals are opening salvos to negotiations. Plenty of evidence from Trump 1.0 suggests this could be the case.

U.S. tariffs, taxes, government spending and the resulting debt and deficits matter for U.S. bond yields. Rising U.S. bond yields caused by unsustainable debt and deficits pose a risk to U.S. equity markets. They also pose a global threat, given the significance of U.S. bond yields and currency to the world. Corporations and share prices can deal with higher bond yields due to modest inflation. It's even easier to take if higher bond yields are driven by gains in real economic growth. Higher bond yields for any other reason spell trouble. One anxiety-producing reason could be a U.S. fiscal house in disarray. There is room for movement on many fronts around this topic. The newly established and highly touted Department of Government Efficiency (DOGE) is a nod to some focus on improving fiscal behaviours. We believe it would take time for a crisis to develop. Few alarm bells are ringing in the capital markets, but an amber light could pop up on the dash.

Given that the mix of positives outweighs the negatives, U.S. equity markets have been on a tear, leaving valuations for the S&P 500 elevated. However, the numbers are skewed by the influence of the Magnificent Seven companies (Apple, Nvidia, Microsoft, Alphabet, Amazon, Meta and Tesla). Combined, these stocks are currently trading at 33 times forward earnings. However, Tesla sits at 100 times and Nvidia at 41 times, while the others range between 20 times earnings for Alphabet and 31 for Microsoft. Two takeaways: not all companies (even the big names) are expensive; and some companies are expensive for a reason (they are outstanding businesses).

Outside of these mega-companies, valuations are attractive in other parts of the U.S. stock market. The S&P 500 is regarded as one of the best gauges of the entire equities market because of its diversity and depth. Using the equally weighted version of the S&P 500, a typical S&P 500 stock has a valuation of 20 times earnings, slightly above the longer-run average of 19.

We are not oblivious to the high valuations in some U.S. stocks. Historically, valuations alone are not a useful guide to investment decision-making. Given the positive backdrop, benchmark equity indices shouldn't be trading below their average valuations. When sentiment is awful, and earnings outlooks are terrible, U.S. stocks still trade at 12 times earnings. The extremes skew averages. We aren't at the extremes in all stocks.

The largest U.S. companies are stellar franchises delivering exceptional earnings growth; opportunities can also be found outside these names. Our U.S. equity exposure is not solely to the S&P 500. Our managers allocate across a wide range of sectors and find opportunities in companies of varying sizes. We are disciplined and discerning with our U.S. equity exposure.

The bottom line for equities

As we said in the introduction, our forecasts for asset class returns begin with looking at long-run averages and asking why we might see a deviation. **Normal earnings growth is in the high single digits. Given the positive backdrop, mid-to-high teens earnings growth wouldn't surprise us.** We see the prospect for positive earnings surprises greater than the odds of the opposite.

Valuations are above normal in some markets and more reasonable in others. Earnings growth in the teens, even on extended valuations, can deliver high-single to low-double-digit stock market returns. High earnings growth and continued elevated valuations can deliver another year of exceptional equity market returns.

One of our gut-checks during forecasting is to ask ourselves if we are calling for an outcome that doesn't happen very often. Strings of exceptional years or exceptional years on their own, followed by normal year returns, are not rare. **For the S&P 500, 25 out of the past 96 years have experienced gains of 25% or more, better than a one-in-four hit rate. Additionally, large positive years do not automatically set up for a poor year to follow. There is no discernable relationship across calendar years; the average return after a year of 25% or better is still 8.6%.**

All of this has us overweight equities. In our base case scenario, equities can deliver mid-teens total returns. Our targets are 28,600 for the S&P/TSX Composite and 6,600 for the S&P 500.

Capital Market implications – Fixed income markets

Yield on a U.S. or Canadian government bond can be dissected into three pieces: an inflation component; a real economic growth component; and what is called the term premium.

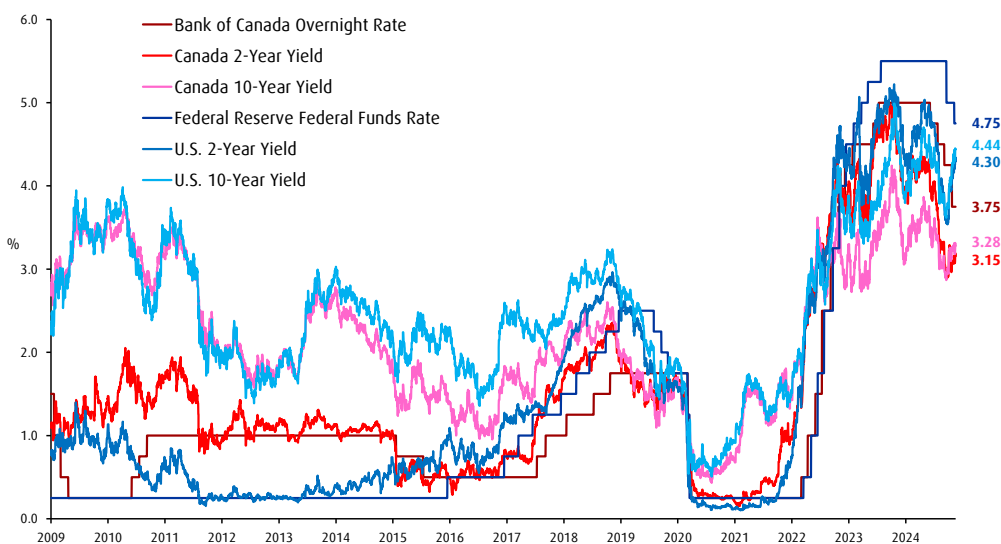
The inflation component is behaving nicely for U.S. and Canadian bond yields. The situation is better in Canada, where cooling inflation is well underway; Canadian bond yields and expectations for our central bank's future moves reflect this. In the U.S., inflation continues to ebb, but not as quickly. There is a risk that the worst of Trumponomics could be inflationary.

Similarly, Canadian real economic growth (real GDP) is limping along (poised to pick up on lower rates) but is lagging the juggernaut of U.S. growth.

These two pieces combined have Canadian bond yields well below their U.S. counterparts. This is a negative for savers and the loonie and a positive for the Canadian economy, borrowers, businesses and share prices. **(See Exhibit 6: Canadian and U.S. Bond Yields)**

Exhibit 6: Canadian and U.S. Bond Yields

Canada and U.S. Policy Rates and Selected Bond Yields
January 1, 2009 – November 15, 2024



Source: Bloomberg

The third variable, term premium, is a nebulous concept. It is defined as the extra compensation (higher yield) investors demand in return for holding long-duration bonds rather than rolling over a sequence of shorter-dated securities. It's easier to understand if you think about wanting to be paid more for assuming the risk of loaning someone money for 10 years versus one year.

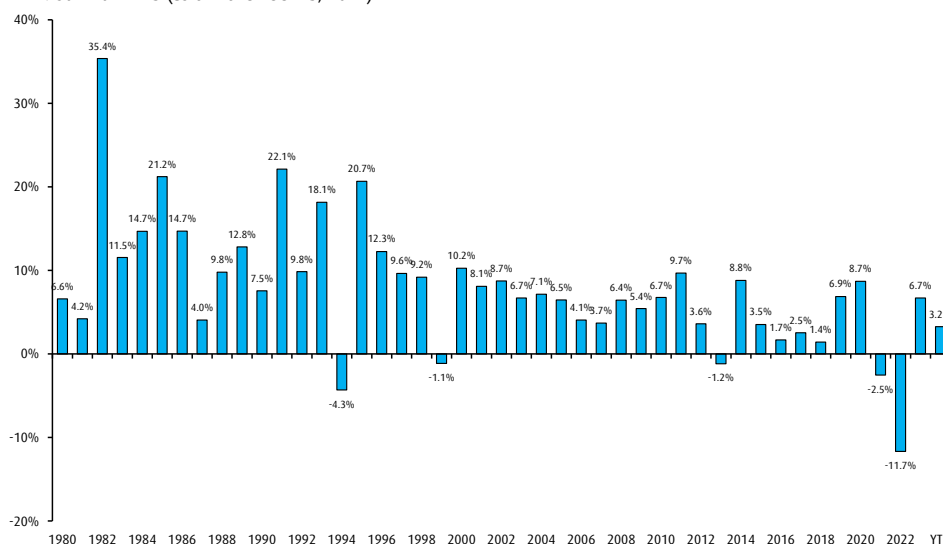
Unfortunately, like some of the best things in finance, the term premium cannot be observed directly; it can only be forecasted, which necessarily brings errors. Nonetheless, estimates show that the term premium in U.S. government bonds is drifting higher. This could be due to rising long-term inflation expectations, which account for about half the increase in term premiums. The other likely suspect is rising U.S. debt and deficits. On this score, if the president-elect enacts all his promises, a Trump presidency is expected to drive higher inflation, deficits and growth than would otherwise be the case. U.S. bond yields have risen on these prospects.

If inflation and growth go higher, a textbook response from the U.S. Federal Reserve (the Fed) would be to keep interest rates higher. Given all these what-ifs, volatility in the bond market has been elevated. **(See Exhibit 7: Bonds - Volatile, But Back on the Job)**

Exhibit 7: Bonds - Volatile, But Back on the Job

FTSE Canada Universe Bond Index Annual Total Return

1980 – 2024 YTD (as of November 15, 2024)



Source: Morningstar (1980 – 2023), Bloomberg (2024 YTD).

Given our views on inflation, **we expect the Bank of Canada to lower the overnight rate to 2.5% from the current 3.75% level by June 2025 and then hold. For the Fed, we expect a decline from the current 4.75% to 3.5% by the end of 2025.**

Examining the current level of Canadian and U.S. 2-year and 10-year bond yields (3.15% and 3.28% for Canada, 4.31% and 4.44% for the U.S.), we see room for yields to fall as central banks continue to have room to lower benchmark rates.

We forecast interest rates available on cash balances will be in the high 2% range by the end of 2025.

In our base case scenario, **our end-of-2025 call is for the yield curve to steepen, with Canadian 2-year bond yields of 2.75% and 10-year bond yields at 3%. This should drive a total return from the broad Canadian fixed income market in the 4% range.**

Currency outlook

The outlook for the Canadian dollar isn't great, but we are more optimistic than many. The different realities for inflation, growth and interest rates between the U.S. and Canada have knee-capped the loonie. **(See Exhibit 8: The Loonie and Interest Rates)**

As a country, we are not alone: the U.S. dollar has been strong against just about all other currencies. Aside from the panic-driven spike during the pandemic, the DXY Index of major currencies against the U.S. dollar sees the greenback at the strongest level in 20 years. Many of these factors are already priced into exchange rates. Given the level of U.S. dollar strength and the speed of the most recent 5% move higher, the U.S. dollar should run into some resistance.

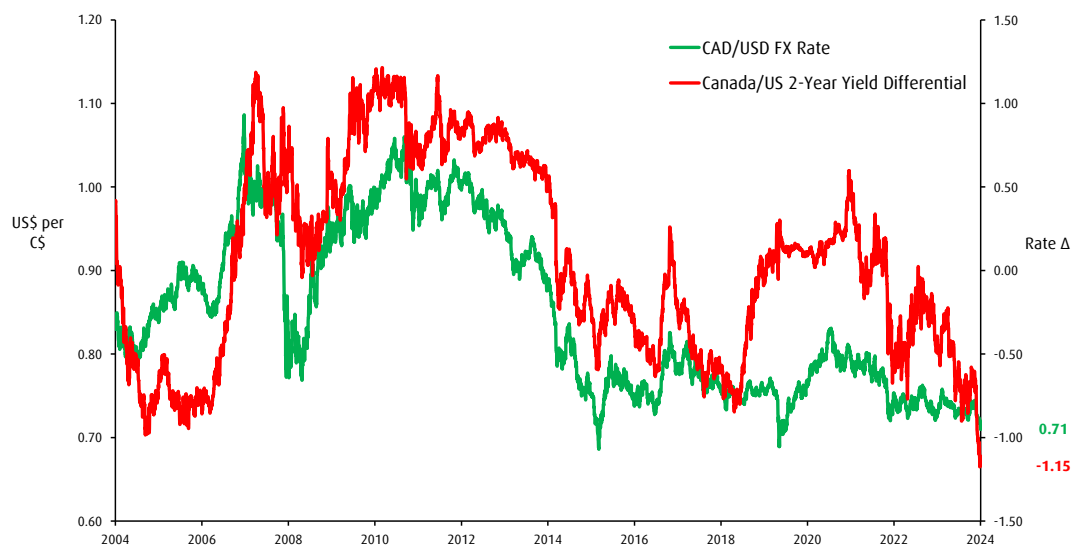
There aren't many fundamental factors that suggest the loonie's fortunes are going to turn around imminently or drastically. But with the very pessimistic sentiment (a lot already embedded in the price), we believe most of the weakness is done.

We expect the loonie to appreciate throughout the year, with an exchange rate of C\$1.35 or US\$0.74 at the end of 2025.

Exhibit 8: The Loonie and Interest Rates

Canada/U.S. 2-Year Yield Differential vs. CAD/USD FX Rate

November 15, 2004 – November 15, 2024



Source: Bloomberg

Our positioning

Our portfolios remain well diversified and balanced. We favour equities over fixed income but see opportunities in cash, bonds, stocks and selected alternative investment strategies that could contribute to return or mitigate risk.

Overall, in our broadest representative portfolios, we are overweight Canadian and U.S. equities, neutral weight to international developed markets (Europe and Japan) and underweight emerging markets.

We engage various active investment managers sourced from across the globe to work on your portfolios. Throughout 2024, we took the opportunity to rebalance into strength to ensure our equity exposures remained prudent. We will continue to deploy this discipline, which will become more important if equity markets continue to advance at a brisk pace.

Specifically, while we maintain a significant weight to U.S. large-cap equities, we have taken steps to trim our exposure to the largest names in the U.S. equity market where momentum and exuberance may have crept in. To accomplish this, in portfolios where we employ a multi-manager approach, we are favouring our active stock-picking managers over the passive index component. Additionally, we deployed money to the dedicated, specialized U.S. small-cap managers who are experts in finding opportunities outside the mainstream.

Within fixed income, we are overweight investment-grade corporate bonds and underweight the lowest-quality borrowers in high yield.

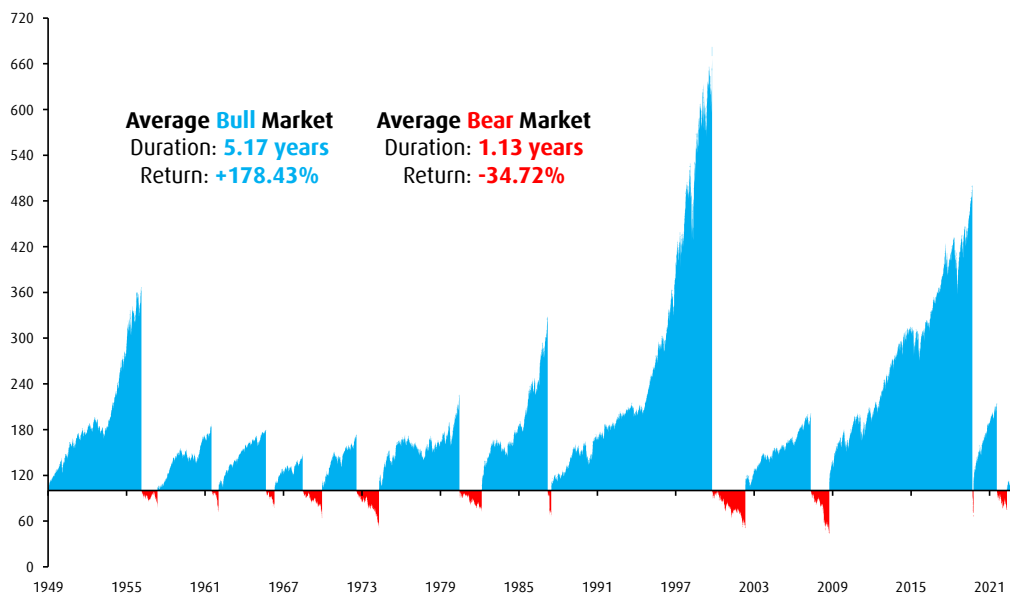
Our fixed income exposure is under the direction of a sophisticated mix of Canadian core bond managers with expertise harvesting gains from volatile bond markets such as we are currently experiencing. To this, we add specialized corporate bond managers, a diversifying global bond manager, and outcome-oriented structured note solutions specifically built for us by BMO Capital Markets. **The current yield from our well-diversified bond positions is very competitive.**

The last word: Bulls outrun bears

The current bull market for the S&P 500 was born on October 12, 2022, making it just over two years old, with a 64% price-only advance to mid-November 2024. Since 1949, the average bull market has run more than five years and gained 178% – we're barely middle-aged in the history of bull markets. **(See Exhibit 9: Bulls Outrun Bears)**

Exhibit 9: Bulls Outrun Bears

S&P 500 Normalized Price Return During Bull and Bear Markets
June 13, 1949 – December 29, 2023



Source: Bloomberg

Just as capital markets can retreat more than they should when things are bad, they can run up higher than expected when times are good. Mountains of research corroborate that trying to time these cycles is impossible. Seasoned investors accept the advice not to panic when markets are way down. Similarly, seasoned investors know that it's also a challenge to keep your head when markets are way up.

Our objective is to be prudent. We look at the situation from that angle and ask whether the current fundamentals support asset prices. We don't run on emotion; we roll with the bunches and punches.



































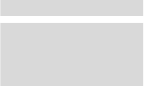




Over the last few years, Canadians have weathered the pandemic and rising inflation. Conflict and political upheavals of many varieties have unsettled our world. Uncertainty is a constant. We accept it and turn it into a strength, surveying all the possibilities and opportunities that uncertainty provides. As long-term fundamental investors, we rely on sophisticated research and market experience to guide our investment strategies. We remain constructive on the investment outlook for 2025.

It's our conclusion that the fundamentals of economic growth, corporate earnings, inflation, bond yields and sentiment remain supportive. Valuations are mixed. Therefore, we continue to rely on diversification across geographies and asset classes – stocks, bonds, cash and alternatives – to meet our clients' individual investing objectives.

Strategy summary

Asset Class outlook

As of November 15, 2024

Category	Economy	Policy	Valuation	Sentiment	Our Positioning			Rationale
					Under	Neutral	Over	
Major Asset Class								
Fixed Income								Fair yields - inflation falling. Central banks are in an easing cycle. Credit spreads are tight.
Equities								Earnings outlooks remain solid with room to beat, margins are healthy, valuations require selectivity.
Equities by Geography								
Canada								Expect outperformance if yields fall and growth picks up. Attractive valuations. Handsome 2025 estimated dividend yield 2.9%
United States								Solid earnings growth. Valuations less attractive, opportunities in active stock selection.
Europe								Geopolitical uncertainty remains. Economy and earnings better than feared. Attractive 3.7% 2025 dividend yield
Japan								Monetary policy a headwind. Export-oriented stock market dependent on global growth.
Emerging Markets								China growth lackluster. Policy stimulus improving. Negative sentiment on politics and geopolitics. Valuations attractive



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