



# Economy and Markets

## Retrospective and Perspective

December 3, 2012

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# Retrospective and Perspective

November – Chippy U.S. equity markets, EU recession and uptick in China metrics

Review

**U.S.** equity markets in November were quite choppy week-to-week, but ended with modest gains for the month of 0.6%. This followed an October S&P 500® Index decline of nearly 2%. Normally, the fourth quarter is one of the stronger seasonal quarters for equities, but not yet. Why?

At least four main domestic factors riled U.S. equities during October and November. At the top of the list were our presidential and congressional elections. These elections unsettled markets; the Dow Jones Industrial Average Index, for example, fell over 450 points in the first two trading days post elections. Second, the lack of clarity regarding how our “fiscal cliff” and longer term fiscal condition get resolved also rattled the markets. Third, corporate America sales and earnings results in the third quarter rose very modestly. Fourth, the devastation from Superstorm Sandy, which left much of the Northeast flooded and without power, carried an economic consequence, as well.

But then came “Black Friday” through “Cyber Monday,” a four day post-Thanksgiving test of consumer spending. Consumers came out and spent. Over the four day period they raised the ante by over 6% from the same period a year ago. Maybe we should not be too surprised, as consumer confidence has been on the rise, housing prices are up nicely, there is some improvement in employment, and stock prices are up almost 15% year-to-date, in spite of October/November weakness.

**Europe** saw their bourses ride higher in November by 2.2% (on top of a 0.8% rise in October), as measured by the STOXX 600 Index, a useful proxy for pan-European stock markets. Europe’s equity markets continue to feed on the confidence that additional funding for Greece was agreed to, that interest rates on Italian and Spanish sovereign debt remain well off their peak levels, and that German leaders remain firm in their resolve to keep the European Union intact. And, importantly, the ECB is on call to take any necessary action.

That said, the economies of France and Germany, which represent nearly half of the Eurozone economy, are dangerously close to recession levels. For the third quarter of 2012, each of these two economies eked out only a 0.2% gain in real GDP. It seems likely, given remaining weaknesses in Greece, Spain, Italy, etc., that at least a modest recession is in the cards for the EU.

TOTAL RETURNS (as of 11/30/2012)	November	Last 3 Months	Year-to-Date
S&P 500® Index	0.58	1.27	14.96
STOXX 600 Index	2.23	4.08	17.07
MSCI Emerging Markets Index	1.27	6.73	12.71
U.S. 10-Yr Treasury	1.17	0.34	5.31

Sources: Bloomberg L.P., BMO Global Asset Management

**China** and the emerging markets continue to play a pivotal role for global growth. In aggregate, the emerging market economies represent 40% of the world’s purchasing power. So growth in those economies is crucial. The IMF projects these economies in total to grow by 5.5% in 2013 – far higher than what is expected from the world’s developed countries.

China, as the second largest economy, struggles to keep growth on track. But recent metrics are encouraging. Export growth, while erratic, climbed in each of the two most recent monthly readings, GDP growth is holding in the 7% range, retail sales have improved, and manufacturing barometers ticked higher, as well. If past is prologue, the newly installed president and premier of China will initiate additional economic growth reforms early in their leadership.

Key Points to Watch:

- 1) Will fiscal cliff issues get resolved – job # 1, 2, and 3!
- 2) Economy could contract in 1st quarter if no big fiscal relief (not good for markets).
- 3) Consumer pace of holiday season – consensus remains strong
- 4) Corporate results need to improve from 3rd quarter.
- 5) Keep an eye on China’s performance and European resolve.

# Spotlight:

## Politics and the Federal Tax Reform: What's at risk for the Municipal Bond Market?

Review

With the re-election of President Obama and no material changes in the House or Senate, Washington looks much the same as it did prior to the long election cycle. This is not to say the lack of change means tax policy regarding the municipal bond market will remain status quo. On the contrary, municipal bond investors have even more reason to track the national political discussions than before.

Tax policy for the \$3.7 trillion municipal bond market is more uncertain now than at any time in recent history. While both political parties generally agree that the need to reduce the federal budget deficit is necessary, how that occurs and over what time frame is the focus of the debate now and into 2013. To be sure, any of the proposed changes to the municipal bond market would have far-reaching ramifications and are more complicated than appear on the surface.

The Federal tax exemption from interest earned on municipal bonds has been in existence for nearly 100 years. This exemption is not written into the U.S. Constitution, thus Congress has the ability to consider revisions to the federal tax code that could impact the status of municipal interest. Some would claim that the current exemption from federal taxation is clearly a favor to the wealthy. The truth is all taxpayers at all income levels derive some benefit from this provision. Public infrastructure including schools, roads, bridges, and sewers are primarily financed from the proceeds of municipal bond issuance. If the tax-exempt nature of municipal bonds is altered in any way, it would likely lead to higher financing costs to municipal borrowers. Higher financing costs generally can only be paid for through higher taxation at the state and local level.

The stability of the municipal bond market is paramount to holding down issuer financing costs. Yet current ideas include limiting the value of the municipal exemption to some determined percentage, such as 28%. Thus if you were in a higher tax bracket than 28%, say 39.6%, the municipal interest you earned would be taxable above the 28% exemption.

Other legislative ideas include curtailing the tax preference for private activity bonds or replacing tax-exempt bonds with tax-credit bonds, or bringing back taxable Build America Bonds from a few years ago with a lesser federal subsidy rate.

The other significant political debate is what happens to the top marginal income tax rates. There may be a resolution on this before year-end as part of the fiscal cliff debate among members of the lame duck Congress. There is a strong push for top tax rates to rise. All other things being equal, this would favor tax-exempt bonds and would tend to increase an already healthy level of demand for municipal bonds.

At the state gubernatorial level, the Republican Party now controls 30 of the 50 states. Among the states, a renewed focus on fiscal prudence was evident at the ballot box, as roughly half of new borrowing requests were denied. Despite the need for infrastructure investment, the election results illustrate the high hurdle in place for most municipalities to garner taxpayer approval for any new projects.

Perhaps the most significant ballot approval came in the form of Proposition 30 in California. Fifty four percent of state voters approved a tax rate increase for those earning over \$250,000. For taxpayers earning more than \$1,000,000, the new marginal tax rate is 13.3%, the highest rate in the nation. In addition, all Californians will see the state sales tax rise by an additional 0.25%. These new tax initiatives may demonstrate the willingness of voters to approve tax increases targeted to avoid deep cuts in schools. We will wait to see if this willingness to withstand higher taxes to help solve widespread fiscal problems is a trend that spreads to other states.

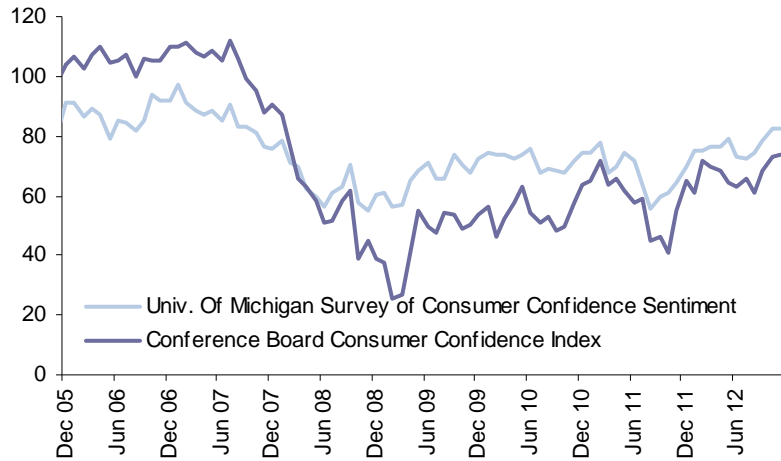
Even with all the uncertainty surrounding the future status of municipal interest, investors have continued to pour money into municipal bonds and bond funds as the hunt for better after-tax yields seems endless. So far this year, investors who have accepted more credit risk and lengthened maturities have been rewarded with superior returns. Of course, this is exactly the type of behavior encouraged by the Fed's zero interest rate policy. Most likely, as long as the Fed remains on hold and yields are high enough to compensate for credit risk, money will continue flow into municipal bonds.

# Highlighted Charts

Strong consumer confidence propelled sales and economic growth. As consumers feel better about the economic outlook, they are reducing savings and increasing their debt.

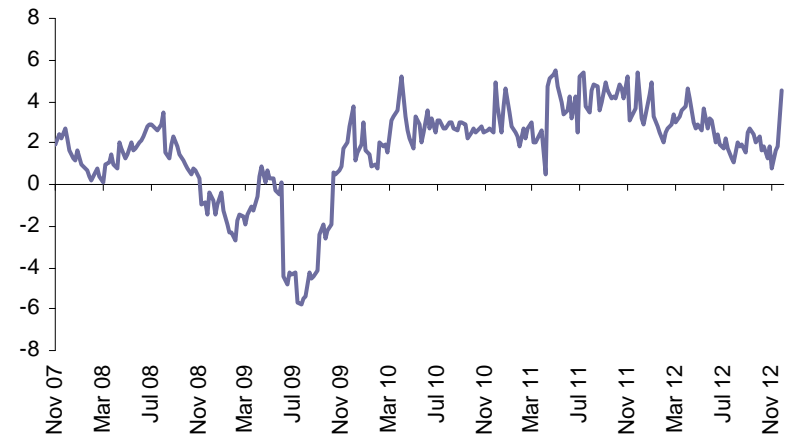
Review

**Consumer Confidence**



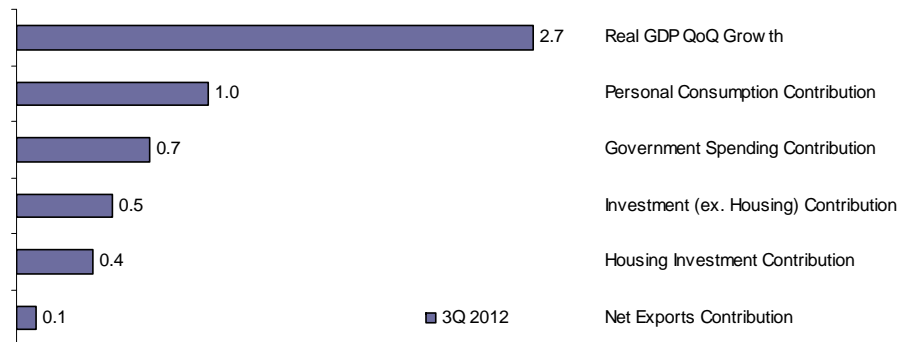
Sources: Bloomberg L.P., BMO Global Asset Management

**Same Store Weekly Sales YoY**



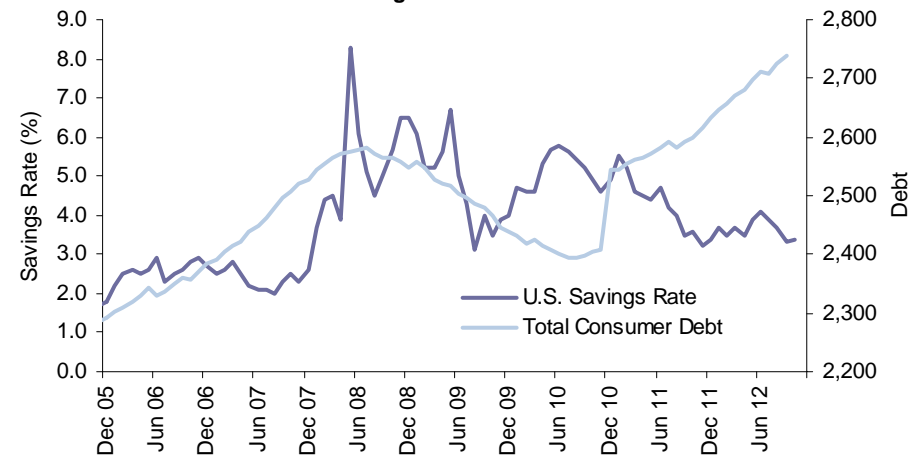
Sources: Bloomberg L.P., BMO Global Asset Management

**Real GDP QoQ Growth and Components Contribution**



Sources: www.BEA.com, BMO Global Asset Management

**Savings Rate and Debt**



Sources: Bloomberg L.P., BMO Global Asset Management

# Market Performance Summary

As of November 30, 2012

Review

## EQUITIES (% Returns)

### U.S. Large Cap Equities

	1-Mo	3-Mo	6-Mo	1-Yr	3-Yrs	5-Yrs	10-Yrs	1Q 2012	2Q 2012	3Q 2012	YTD 2012	2011
S&P 500® Index	0.58	1.27	9.32	16.14	11.25	1.34	6.36	12.59	-2.75	6.35	14.96	2.11
Dow Jones Industrial Average Index	-0.12	0.18	6.54	11.11	10.93	2.33	6.57	8.84	-1.85	5.02	9.38	8.38
Russell 1000® Index	0.82	1.68	9.44	16.28	11.70	1.61	6.83	12.91	-3.10	6.32	15.31	1.54
Russell 1000® Growth Index	1.69	0.68	7.66	15.03	12.58	3.11	6.81	14.70	-4.00	6.13	15.38	2.69
Russell 1000® Value Index	-0.01	2.66	11.25	17.52	10.81	0.02	6.72	11.13	-2.19	6.52	15.20	0.42

### U.S. Mid Cap Equities

Russell Midcap® Index	1.69	2.83	9.57	14.95	14.60	3.14	10.06	12.95	-4.19	5.63	15.08	-1.50
Russell Midcap® Growth Index	2.28	2.03	7.51	12.40	14.79	3.07	9.55	14.53	-5.52	5.42	14.08	-1.54
Russell Midcap® Value Index	1.21	3.61	11.17	17.06	14.47	3.08	10.19	11.42	-3.25	5.84	15.61	-1.36

### U.S. Small-Mid Cap Equities (SMID)

Russell 2500™ Index	1.60	3.25	10.12	15.42	14.78	3.25	-	13.04	-4.12	5.63	15.16	-2.75
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### U.S. Small Cap Equities

Russell 2000® Index	0.53	1.58	8.68	13.09	13.85	2.82	8.74	12.44	-3.47	5.25	12.35	-4.17
Russell 2000® Growth Index	0.87	0.71	7.81	11.37	15.04	3.16	8.83	13.32	-3.92	4.87	11.61	-2.86
Russell 2000® Value Index	0.42	2.80	9.97	15.57	13.05	2.69	8.77	11.74	-2.94	5.72	13.78	-5.37

### International Equities

MSCI ACWI ex USA Index (Devlp. & EM)	2.10	5.94	17.55	11.76	3.17	-4.36	7.92	10.37	-7.20	7.30	13.00	-12.21
MSCI EAFE Index (Developed Markets)	2.42	6.32	18.16	12.61	2.97	-4.73	7.51	10.86	-7.13	6.92	13.68	-12.14
MSCI European Monetary Union Index (in €)	2.93	5.56	20.46	16.13	2.31	-6.59	3.59	9.42	-5.86	7.99	16.38	-15.06
MSCI AC Asia Pacific Index	2.35	6.63	12.39	12.83	4.59	-2.71	8.95	12.01	-6.74	5.56	12.44	-15.11
MSCI Emerging Markets Index	1.27	6.73	12.63	11.35	4.35	-1.79	15.57	14.07	-8.89	7.74	12.71	-18.42

### Technology and Growth Stocks

NASDAQ Composite Index	1.39	-1.43	7.30	16.41	13.24	3.60	8.30	18.98	-4.76	6.54	17.01	-0.79
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## ALTERNATIVES (% Returns)

	1-Mo	3-Mo	6-Mo	1-Yr	3-Yrs	5-Yrs	10-Yrs	1Q 2012	2Q 2012	3Q 2012	YTD 2012	2011
DJ UBS Commodity Index	0.05	-2.18	11.29	-2.22	1.61	-3.81	4.87	0.89	-4.55	9.69	1.59	-13.32
MSCI ACWI Commodity Producers Index	-2.36	0.96	8.86	-5.87	-2.02	-5.91	9.46	4.79	-10.76	6.90	-3.22	-13.84
Wilshire U.S. REIT Index	-0.70	-3.93	2.29	14.55	15.14	-1.19	6.18	9.87	2.82	-0.99	9.92	5.35
S&P Global REIT Index	-0.19	0.09	8.92	17.19	11.35	-3.90	5.40	9.90	1.98	2.60	15.66	-2.65
S&P Global Infrastructure Index	-1.33	2.94	10.73	9.85	4.91	-4.84	9.16	6.85	-2.32	4.63	9.45	-0.21

Highlighted items represent either the best- or worst-performing equity sector for the period.

Total returns for periods of one year or more are annualized. MSCI indices performance is net of foreign taxes on dividends. Sources: Bloomberg L.P., BMO Global Asset Management



# Market Performance Summary

As of November 30, 2012

Review

## U.S. FIXED INCOME (% Returns)

	1-Mo	3-Mo	6-Mo	1-Yr	3-Yrs	5-Yrs	10-Yrs	1Q 2012	2Q 2012	3Q 2012	YTD 2012	2011
Barclays U.S. Aggregate Index	0.16	0.49	1.99	5.51	5.68	6.04	5.41	0.30	2.06	1.58	4.36	7.84
Barclays U.S. Interm. Gov/Crd Index	0.30	0.69	1.94	4.81	4.71	5.25	4.86	0.61	1.48	1.40	3.99	5.80
Barclays U.S. Corporate Index	-0.16	1.84	5.37	12.24	8.72	7.92	6.66	2.08	2.52	3.83	9.89	8.15
Barclays U.S. Treasury Index	0.52	0.04	0.57	3.43	5.07	5.51	5.06	-1.29	2.83	0.57	2.44	9.81
Barclays Securitized Index	-0.14	0.01	1.17	3.61	4.74	5.67	5.12	0.74	1.07	1.28	2.86	6.22
Barclays High Yield Index	0.80	3.10	8.54	17.05	12.48	10.05	10.60	5.34	1.83	4.53	14.02	4.98
Merrill Lynch High Yield BB/B Constr. Index	0.75	2.99	8.25	15.71	11.67	8.90	9.27	4.43	1.91	4.45	13.03	5.40
Barclays 1-10 yr Municipals Index	0.91	1.58	2.41	5.93	4.97	5.38	4.58	0.53	1.27	1.41	4.36	7.62
Barclays Global Aggregate Bond Index	-0.01	1.07	3.61	5.37	3.95	5.45	6.43	0.87	0.62	3.27	4.66	5.64
Barclays Global Credit Index	0.47	3.01	7.83	12.37	6.70	6.23	7.41	4.19	0.36	4.75	11.21	4.36

## BOND YIELDS

	Nov 2012	Oct 2012	Sep 2012	Mar 2012	Dec 2011	Nov 2011
Fed Funds Rate (Effective Rate)	0.16	0.18	0.09	0.09	0.04	0.10
3-month Treasury Bill	0.08	0.11	0.09	0.07	0.01	0.00
2-year Treasury Note	0.25	0.28	0.23	0.33	0.24	0.26
5-year Treasury Note	0.62	0.72	0.63	1.04	0.83	0.95
10-year Treasury Note	1.62	1.69	1.63	2.21	1.88	2.07
30-year Treasury Bond	2.81	2.86	2.82	3.34	2.90	3.06
Barclays U.S. Aggregate Index	1.69	1.70	1.61	2.23	2.24	2.41
Barclays Corporate Index	2.69	2.67	2.80	3.41	3.76	3.96
Barclays High Yield Index	7.03	7.10	7.19	7.73	8.66	9.07
Barclays Emerging Markets Index	4.47	4.56	4.69	5.37	6.10	6.19
Barclays Emerging Markets Corporate Index	4.88	4.80	5.10	5.55	6.85	7.00

## INFLATION

	Nov 2012	Oct 2012	Sep 2012	Mar 2012	Dec 2011	Nov 2011
Headline CPI YoY	NA	2.20	2.00	2.70	3.00	3.40
Core CPI YoY	NA	2.00	2.00	2.30	2.20	2.20
Core PCE YoY	NA	1.60	1.60	2.00	1.90	1.70

## OTHER MARKETS

	Nov 2012	Oct 2012	Sep 2012	Mar 2012	Dec 2011	Nov 2011
US\$ / Euro	1.299	1.296	1.286	1.334	1.296	1.345
WTI Crude Oil Price (\$/barrel)	88.9	86.7	93.0	105.3	97.8	97.6
Gold (\$/troy oz)	1,715	1,721	1,772	1,668	1,564	1,746

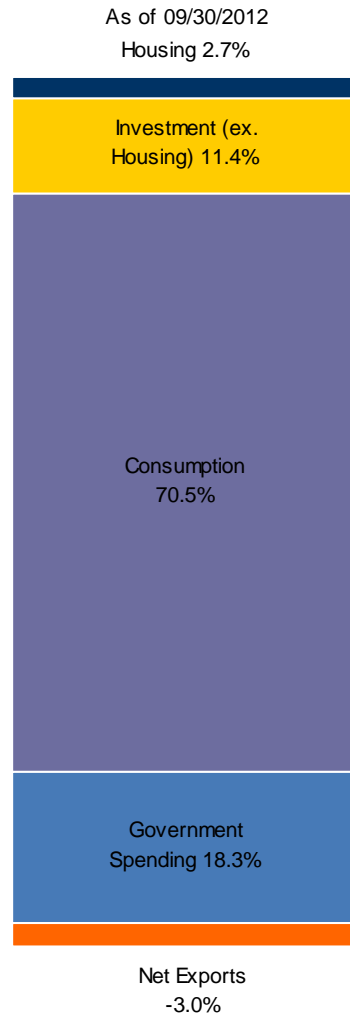
Total returns for periods of one year or more are annualized. Sources: Barclays Capital, Bloomberg L.P., BMO Global Asset Management

# U.S. Economic Growth

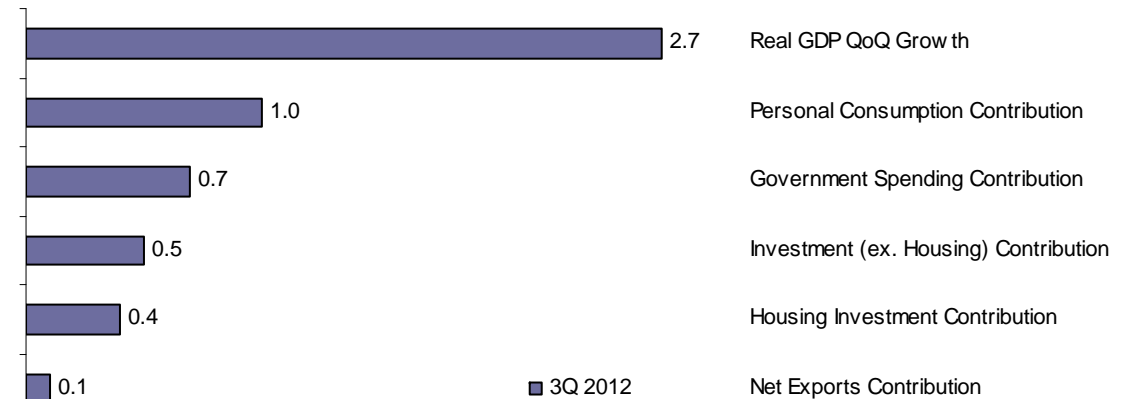
In the third quarter, the U.S. economic growth was revised upward from 2.0% to 2.7%, inventory accumulation accounting for the majority of the revision. While growth was driven mainly by gains in consumer and government spending, all major subcomponents recorded a positive contribution.

Economy

## Components of Real GDP

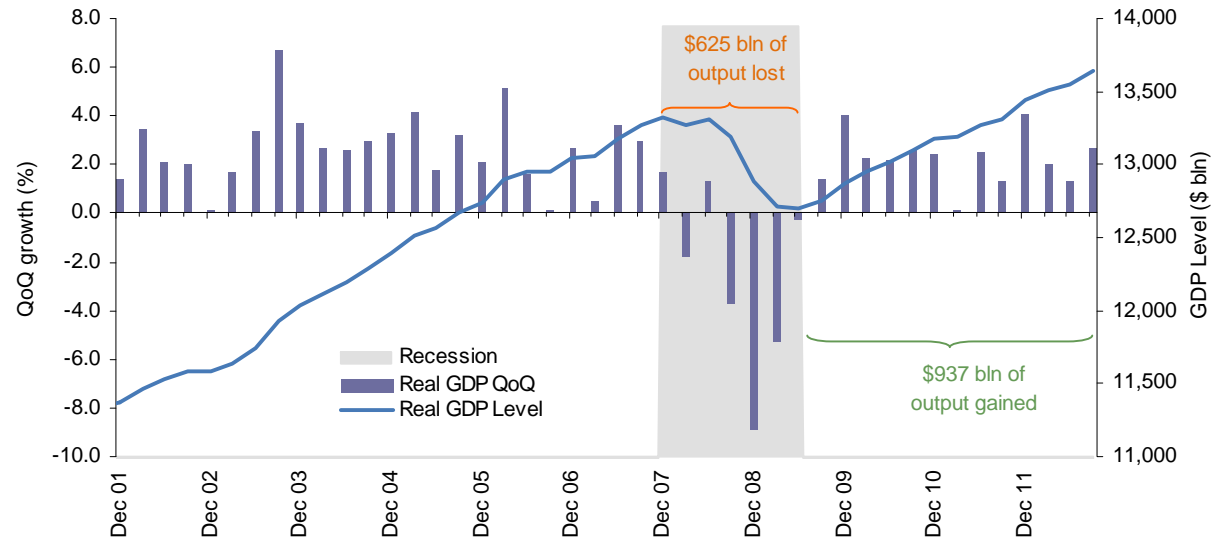


## Real GDP QoQ Growth and Components Contribution



Sources: www.BEA.com, BMO Global Asset Management

## U.S. Real GDP Growth



Sources: Bloomberg L.P., BMO Global Asset Management

Sources: www.BEA.com, BMO Global Asset Management



# U.S. Inflation

Headline inflation (CPI including food and energy) increased by 2.2% in October, 80 basis points more than just three months ago, propelled by an increase in energy and medical care costs. Declining nominal yields, combined with an increase in inflation, have pushed real yields into negative territory.

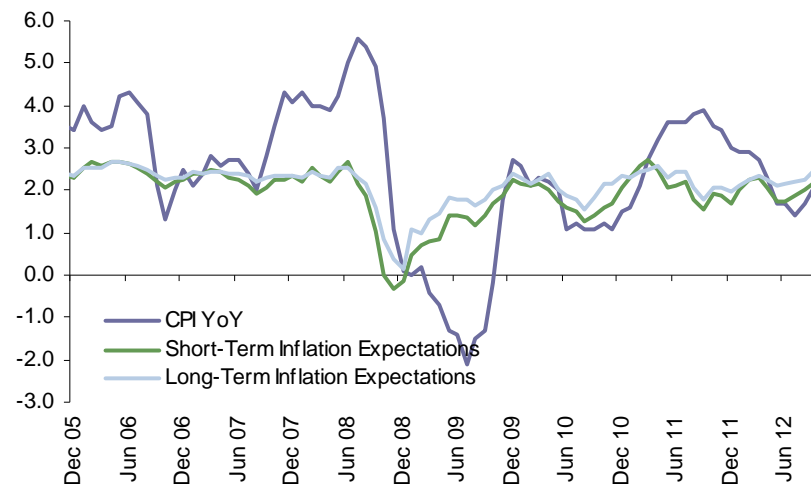
Economy

Urban CPI Components	YoY % Change	Weight in Headline CPI (%)
Headline CPI	2.2	100.0
Food	1.7	14.2
Energy	4.0	10.0
Core CPI (excl. Food and Energy)	2.0	75.8
Housing	1.6	37.9
Transportation	2.0	10.7
Medical Care	3.7	6.5
Recreation	1.3	6.4
Education & Communication	1.5	6.1
Apparel	2.9	3.6
Other Goods & Services	1.9	3.5
Beverages	1.5	0.9

Seasonally adjusted values, as of 10/31/2012

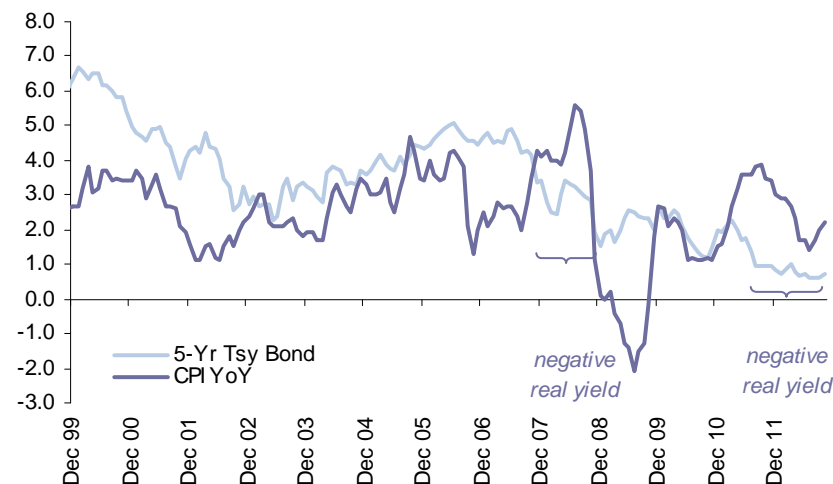
Sources: Bloomberg L.P., BMO Global Asset Management

Inflation Expectations and Nominal CPI



Sources: Bloomberg L.P., BMO Global Asset Management

Headline Inflation and 5-yr Treasury Bond Yield

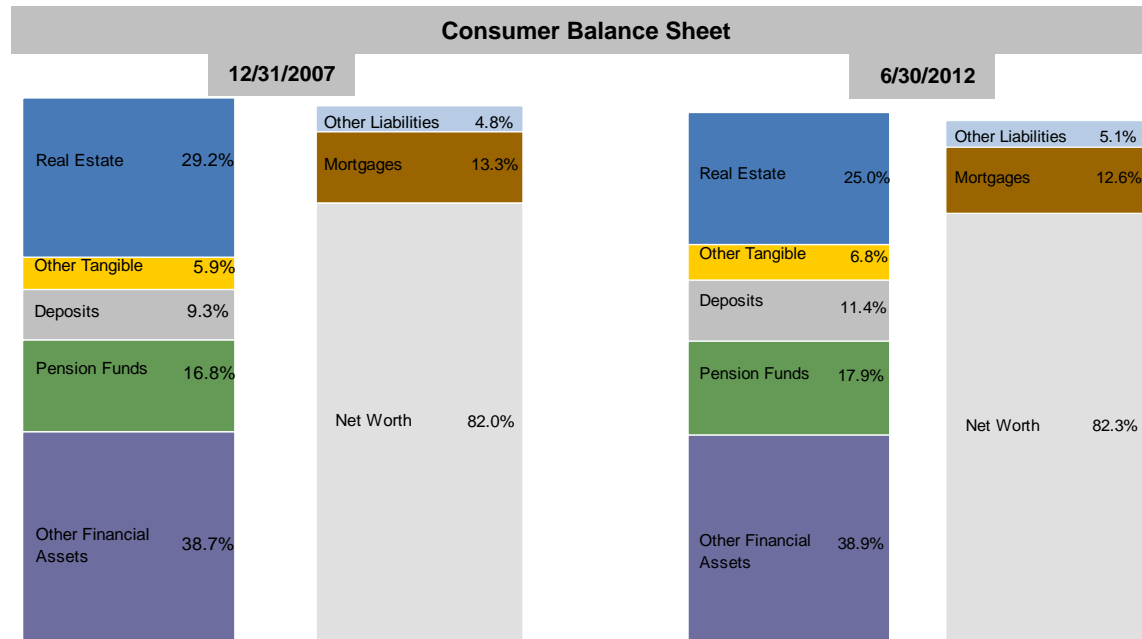
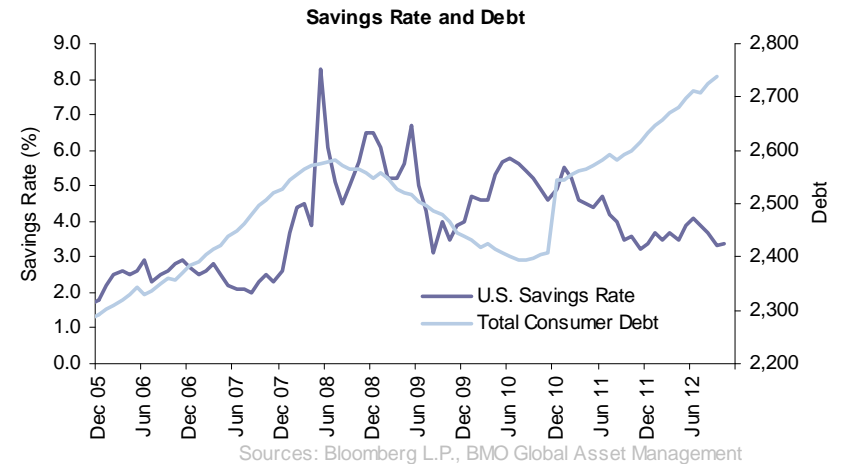
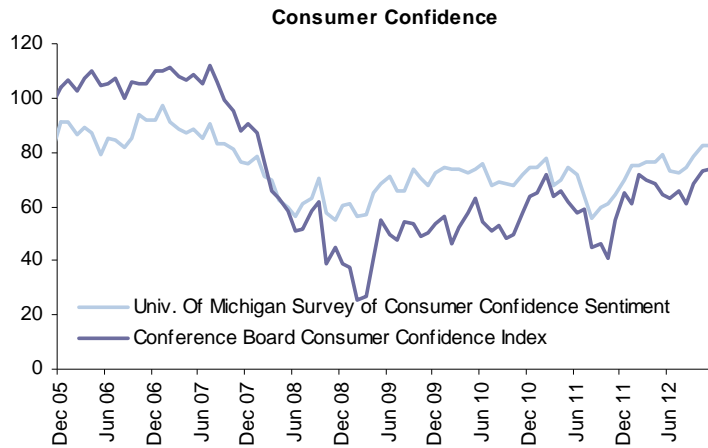


Sources: Bloomberg L.P., BMO Global Asset Management

# U.S. Consumer

As the third quarter GDP growth was propelled by consumer spending, it is not surprising to see an improvement in consumer confidence reports, which have continued to strengthen through the end of November. As they spent more, individuals reduced savings and increased their total debt.

Economy

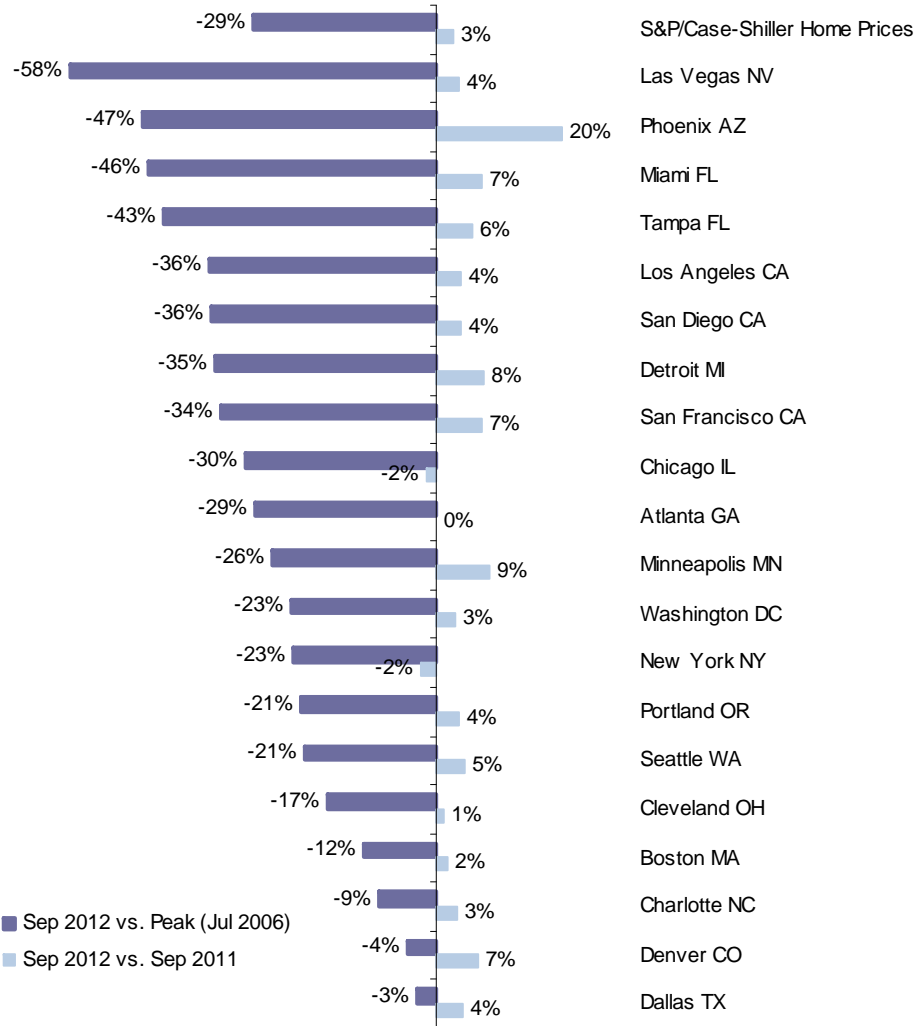


# U.S. Housing Market

Recent housing indicators have brought a wave of optimism, as purchases of existing home increased by 2.1% in October, the S&P/Case-Shiller price index has steadily increased for six consecutive months, and homebuilders confidence has reached the highest level since June 2006.

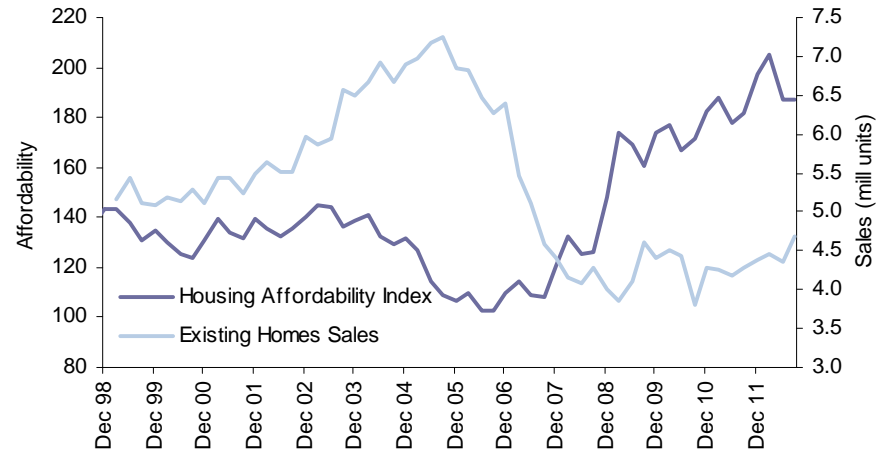
Economy

## U.S. Home Prices



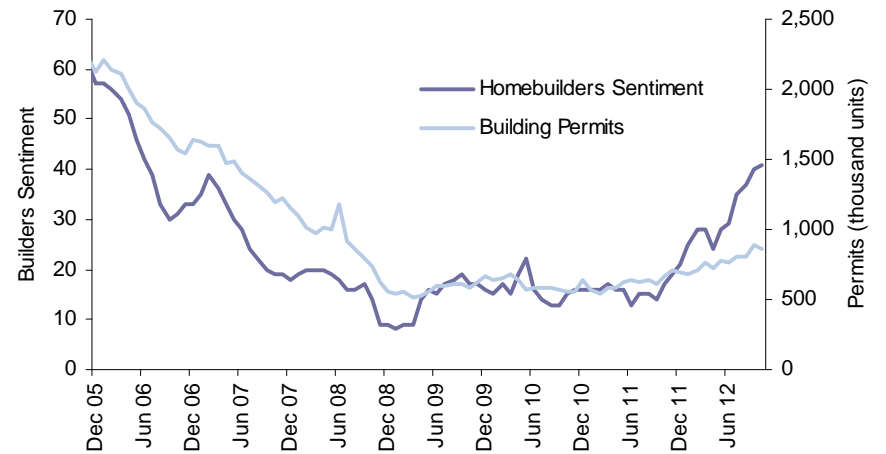
Sources: Bloomberg L.P., BMO Global Asset Management

## Housing Affordability Index and Existing Home Sales



Source: Bloomberg L.P., BMO Global Asset Management

## Homebuilders Sentiment and Building Permits

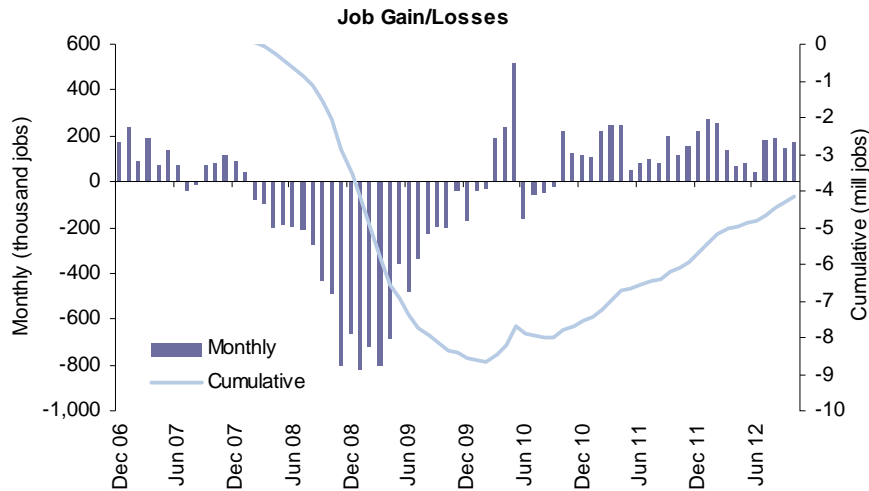


Source: Bloomberg L.P., BMO Global Asset Management

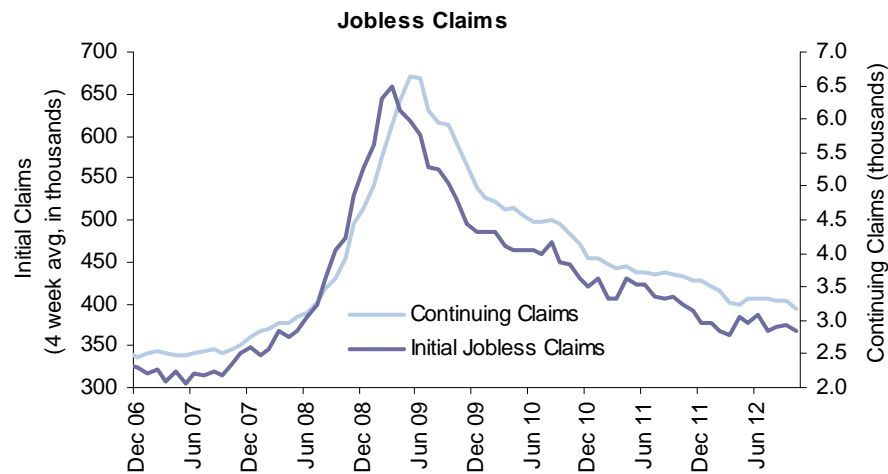
# U.S. Job Gains/Losses

The economy added 171,000 jobs in October, but gains in the prior two months were revised upward. Cumulative job losses since the onset of the 2008 recession stand at 4.1 million. Jobless claims have continued their steady decline and are near levels recorded in mid-2008.

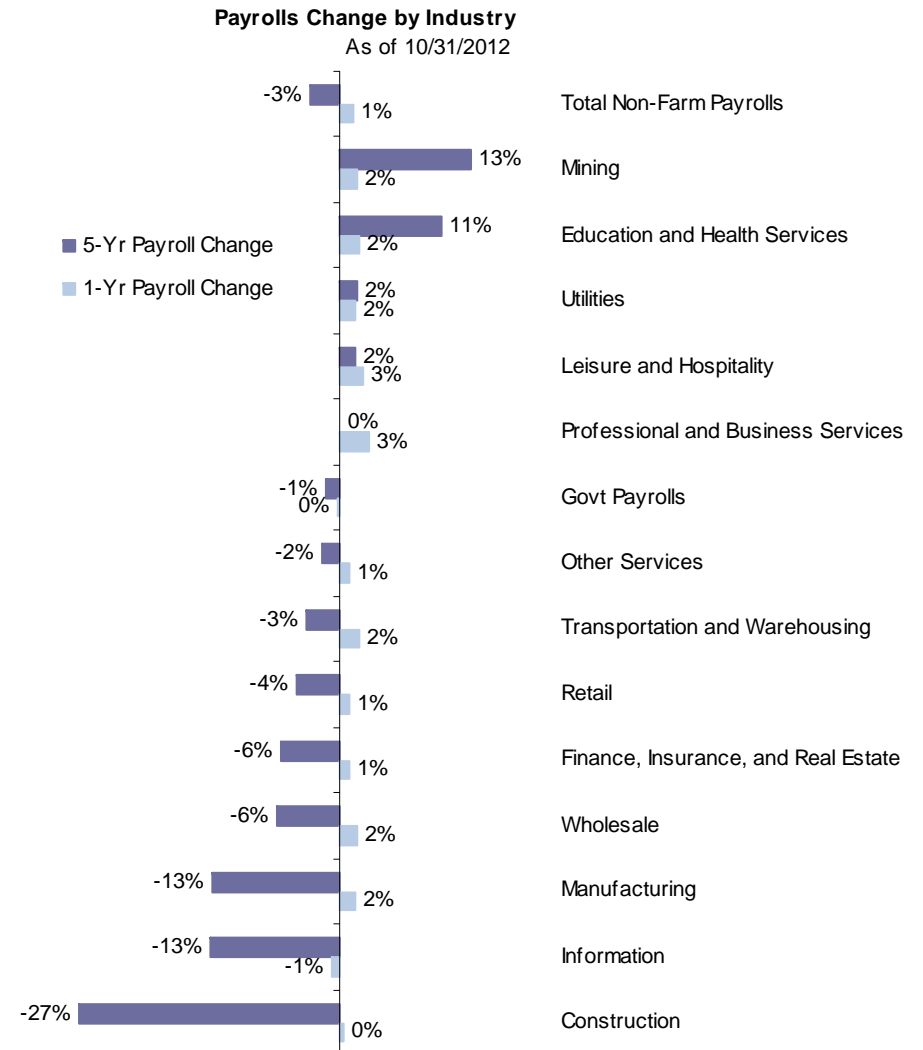
Economy



Sources: Bloomberg L.P., BMO Global Asset Management



Sources: Bloomberg L.P., BMO Global Asset Management



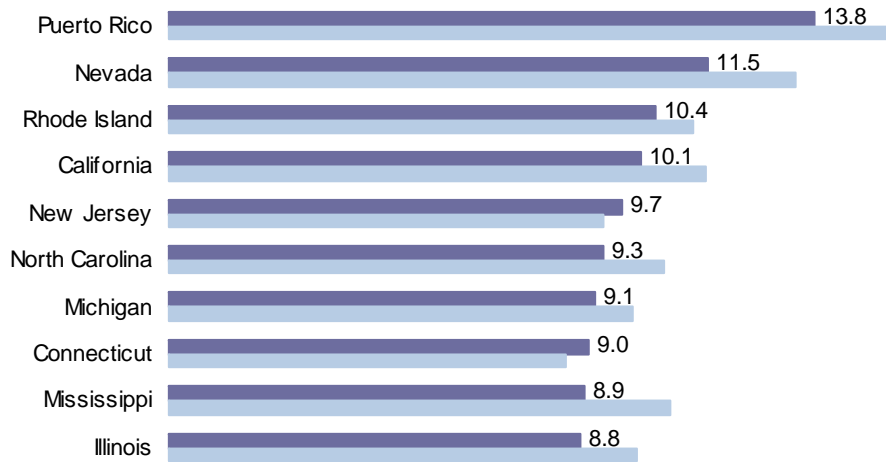
Sources: Bloomberg L.P., BMO Global Asset Management

# U.S. Unemployment

The unemployment rate inched up to 7.9% in October. The decline in unemployment from 8.3% in July to 7.8% in September was primarily due to workers leaving the workforce. The duration of unemployment remains stubbornly high.

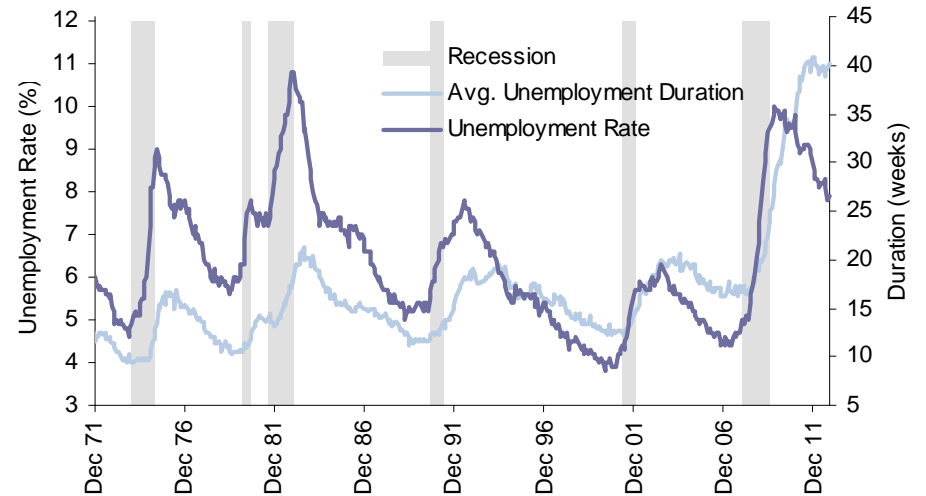
Economy

**Unemployment Rate  
Worst 10 States**



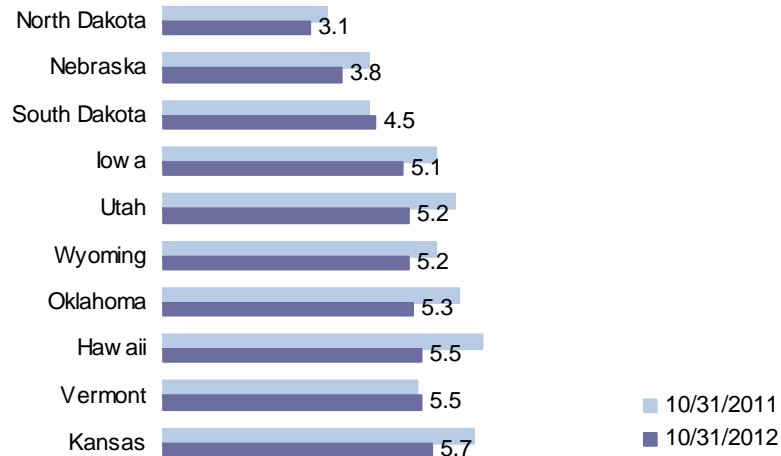
Sources: Bloomberg L.P., BMO Global Asset Management

**Unemployment Rate and Duration**



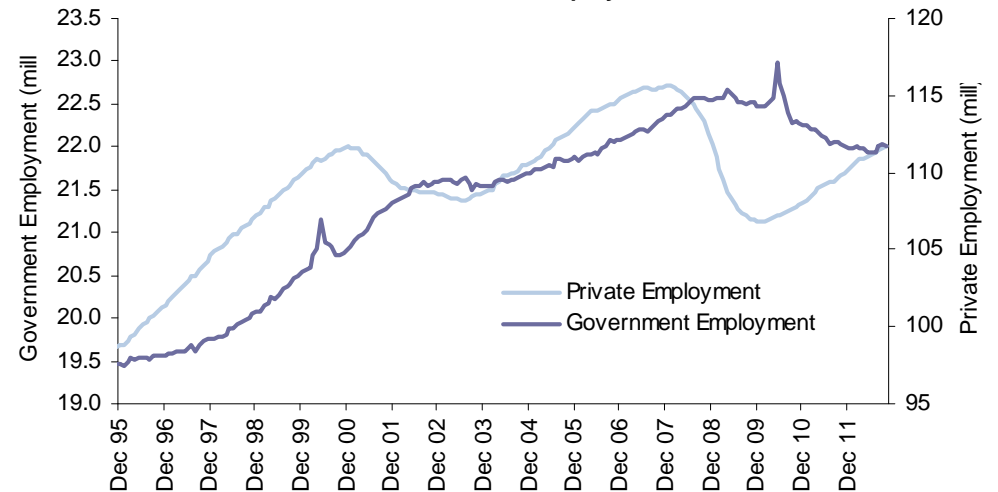
Sources: Bloomberg L.P., BMO Global Asset Management

**Best 10 States**



Sources: Bloomberg L.P., BMO Global Asset Management

**Government and Private Employment**



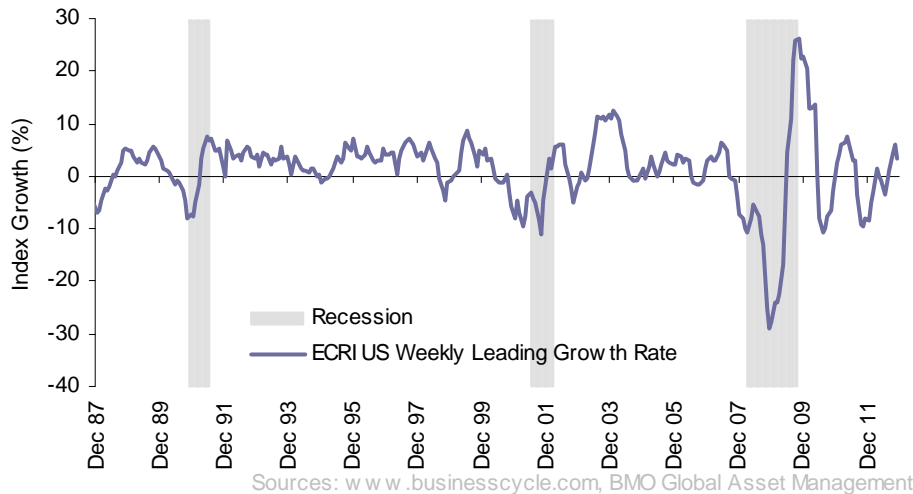
Source: Bloomberg L.P., BMO Global Asset Management

# Other U.S. Economic Indicators

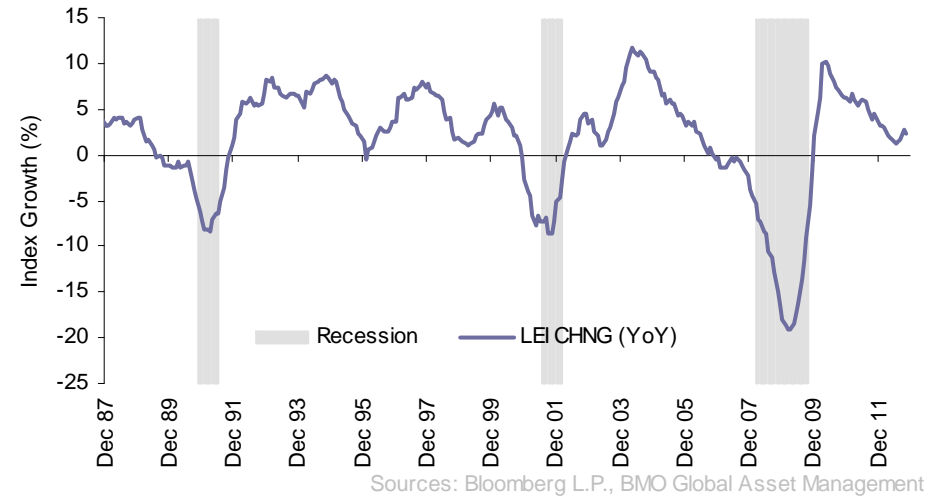
Recent leading economic indicators have increased slightly. Chicago Fed National Activity Index affirms current growth is below its trend-line average, approaching its lowest point since the recession.

Economy

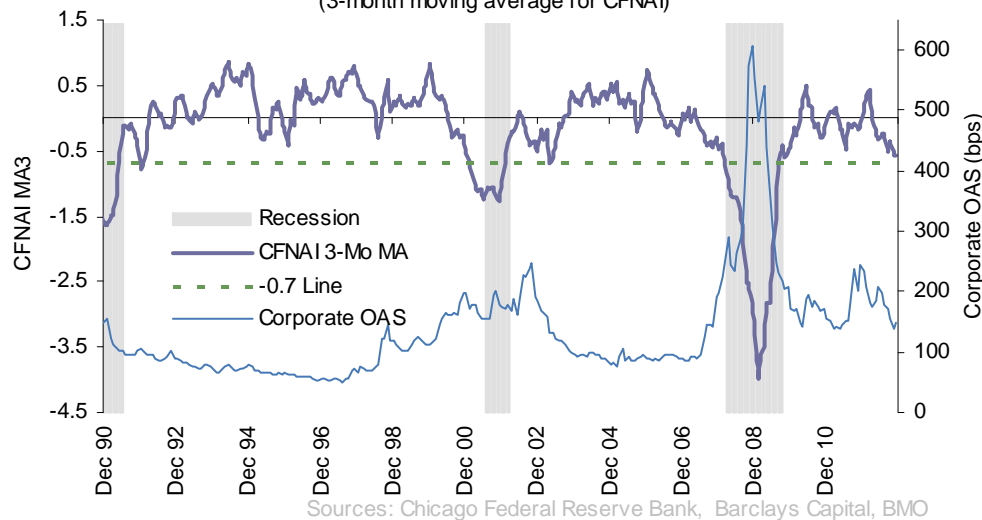
**Economic Cycle Research Institute (ECRI) Weekly Leading Index**



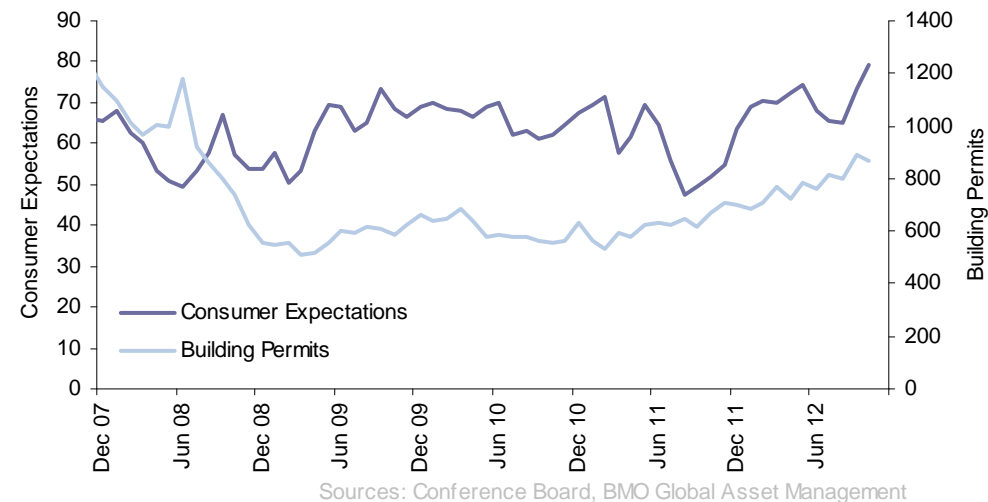
**Conference Board Leading Index Growth**



**Chicago Fed National Activity Index (CFNAI) and Credit Spreads**  
(3-month moving average for CFNAI)



**Leading Index Selected Components**

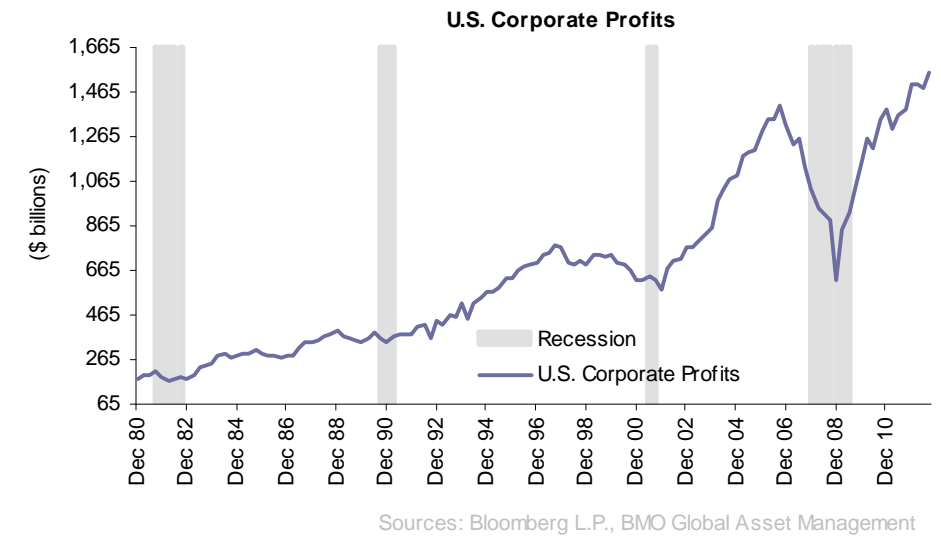
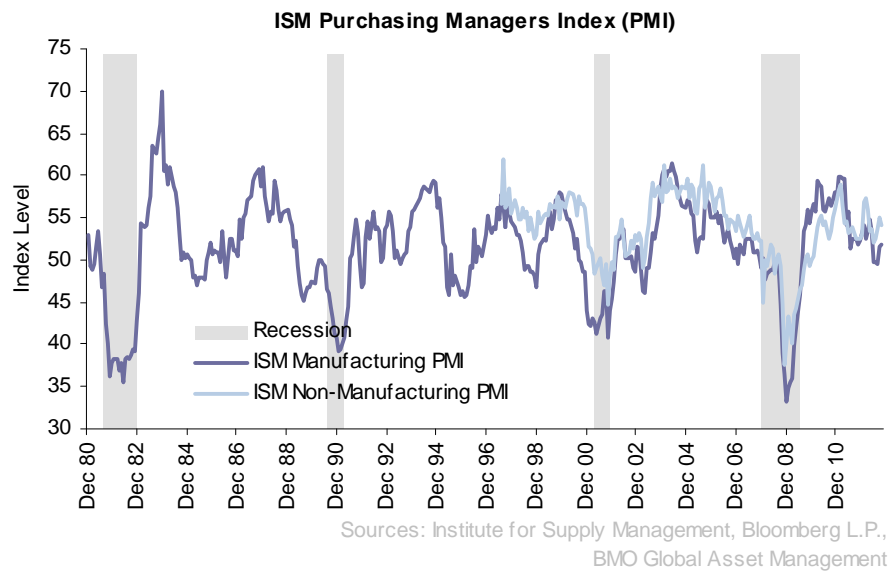
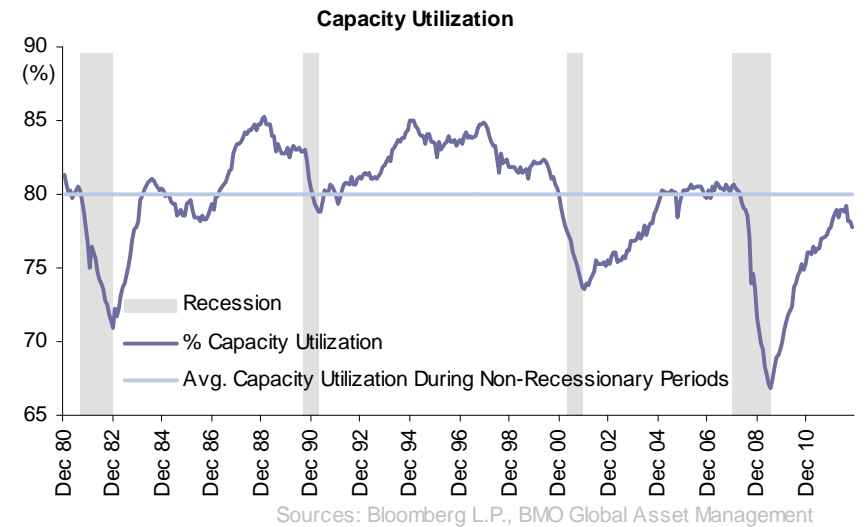
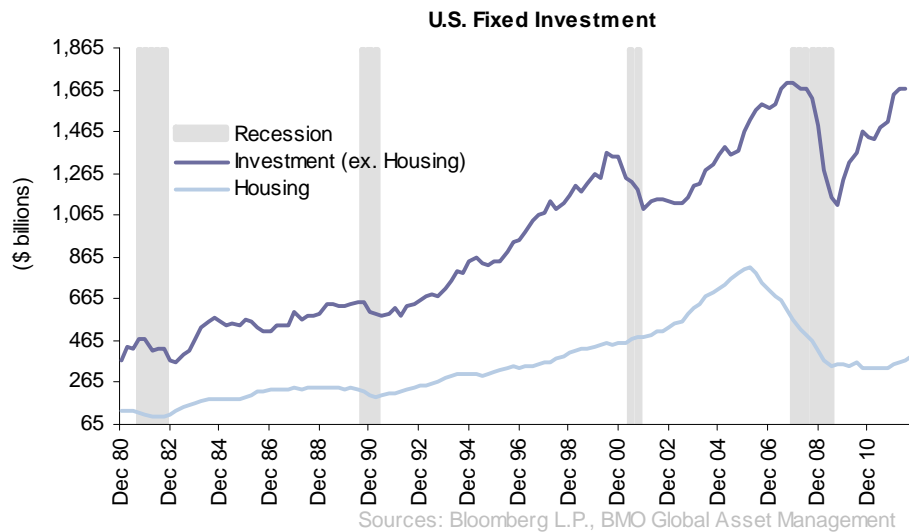




# U.S. Business Activity

Housing investment level remains weak, but other fixed investment activity has steadily increased to pre-recession levels. Capacity utilization, while close to average during non-recessionary periods, has been trending downward since August. Corporations have reported solid profits.

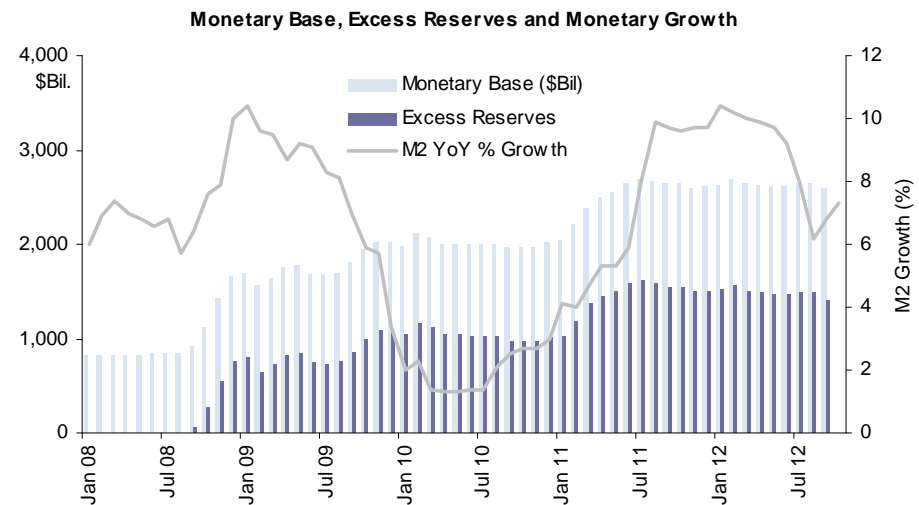
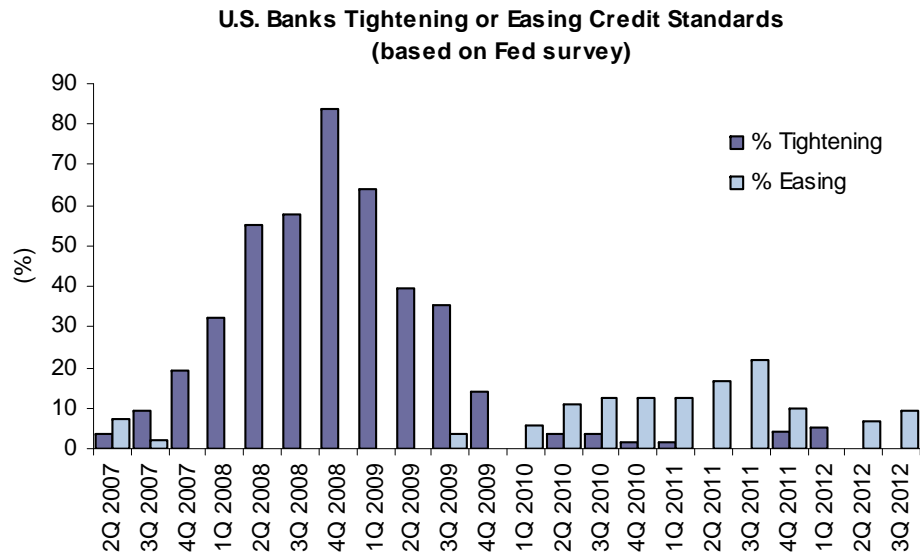
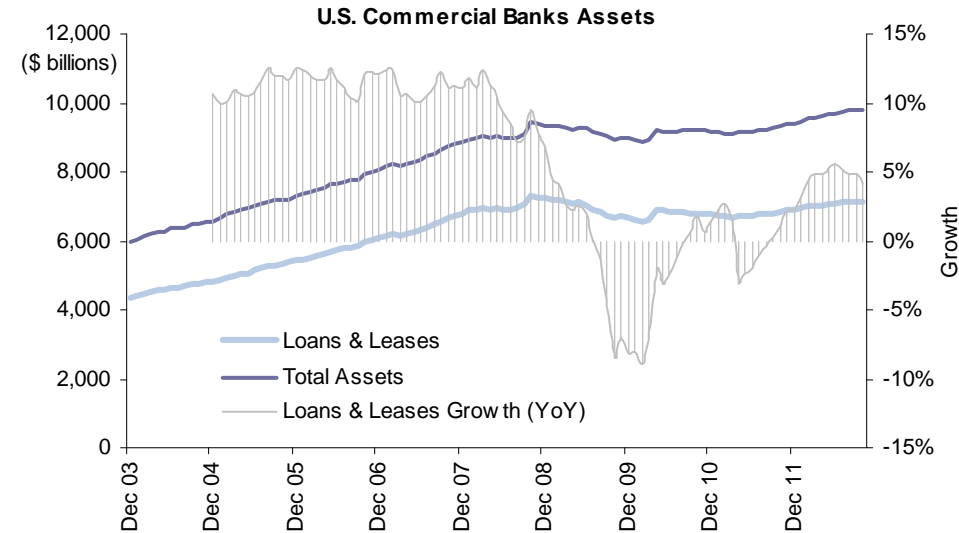
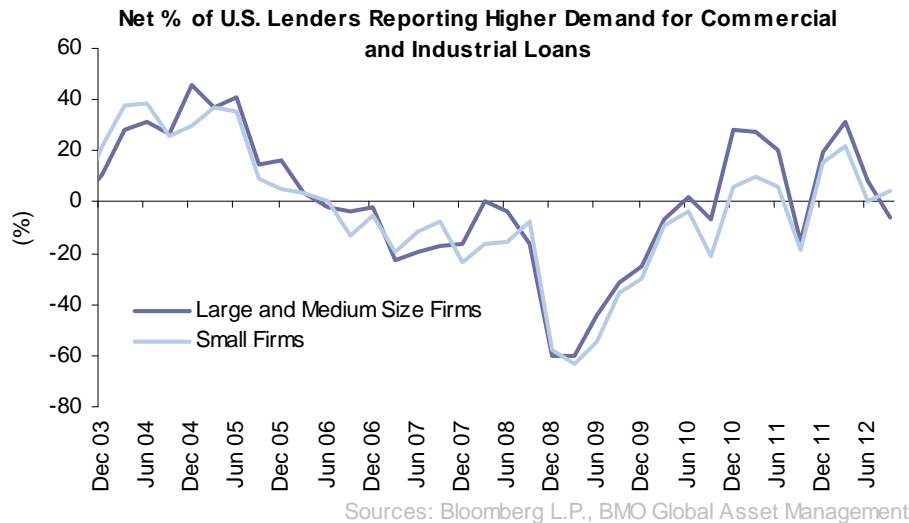
Economy



# U.S. Lending and Banking Activity

Demand for commercial and industrial loans has decreased, although banks are easing credit standards. Commercial banks recorded a slow but steady growth in total loans and leases. Monetary stimulus remains in excess reserves.

Economy

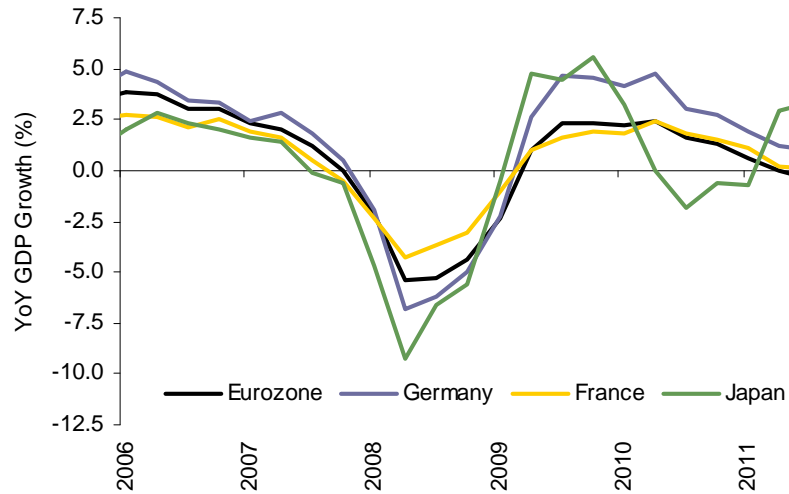


# World Economic Growth and Inflation

Several European economies have slipped into recession; Germany and France have avoided downturns. Economic growth slowed in Brazil and India in the first quarter of 2012. World inflation has been declining slightly since the end of 3Q 2011.

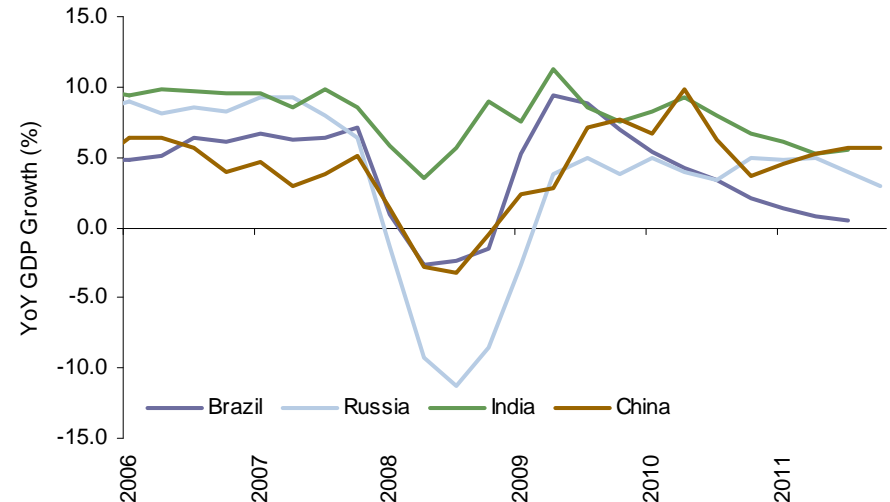
Economy

Real GDP Growth for Developed Countries



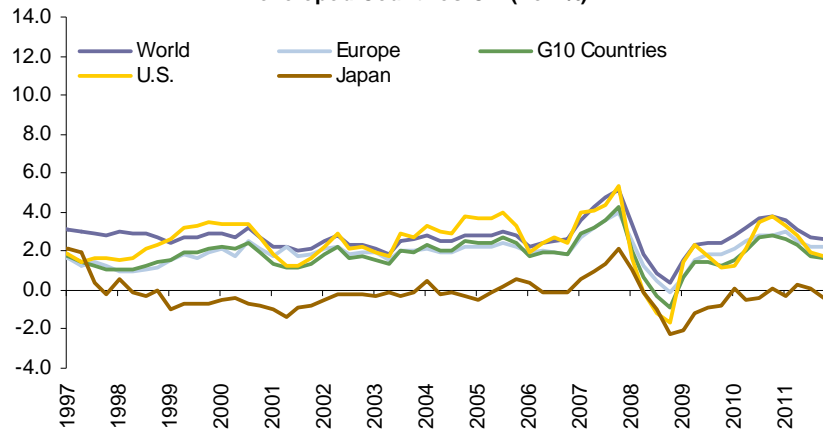
Sources: Bloomberg L.P., BMO Global Asset Management

Real GDP Growth for BRIC Countries



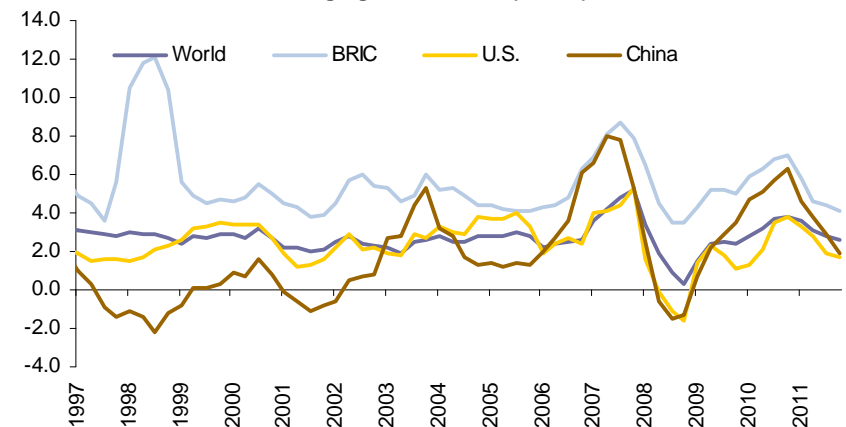
Sources: Bloomberg L.P., BMO Global Asset Management

Developed Countries CPI (YoY %)



Sources: Bloomberg L.P., BMO Global Asset Management

Emerging Markets CPI (YoY %)



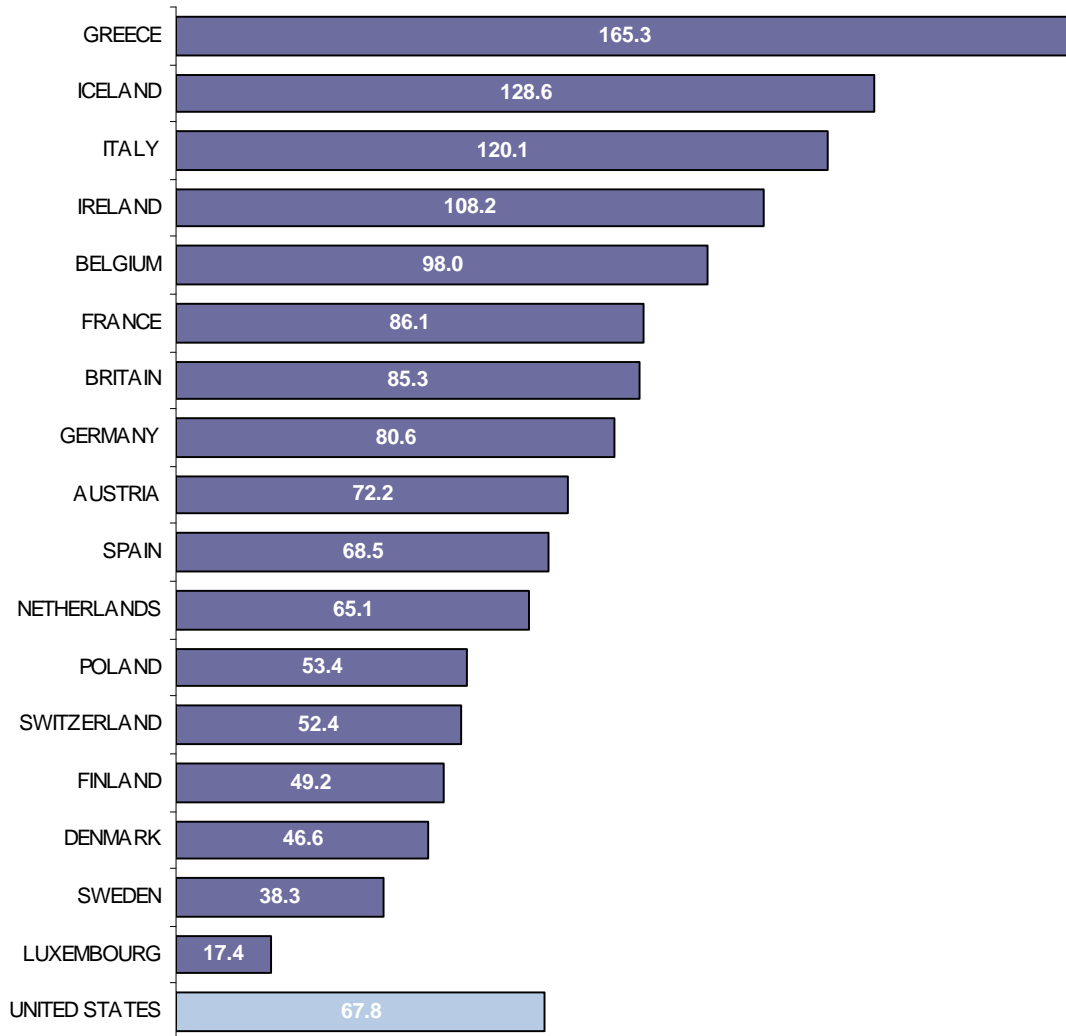
Sources: Bloomberg L.P., BMO Global Asset Management

# European Economies

Many European economies are struggling, being hampered by recession, high debt-to-GDP ratios and high sovereign yields. Yet recent yields show less concern about the European governments' ability to restrain spending.

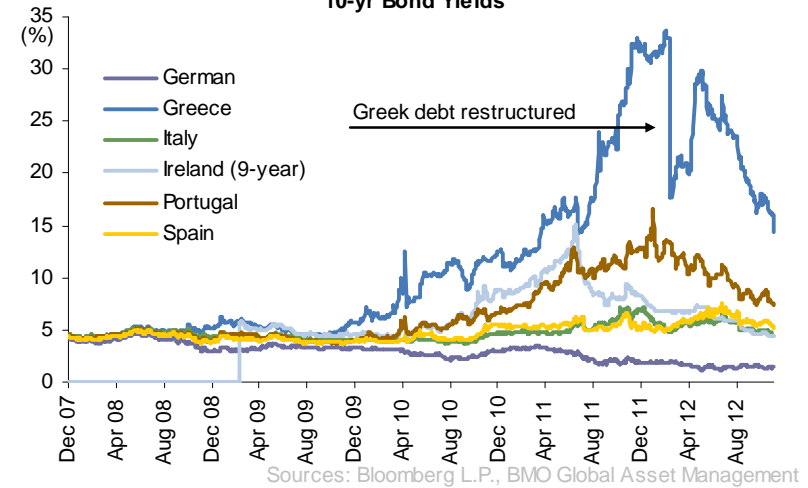
Economy

**Eurozone**  
Percentage Debt to GDP by Country on 12/31/2011

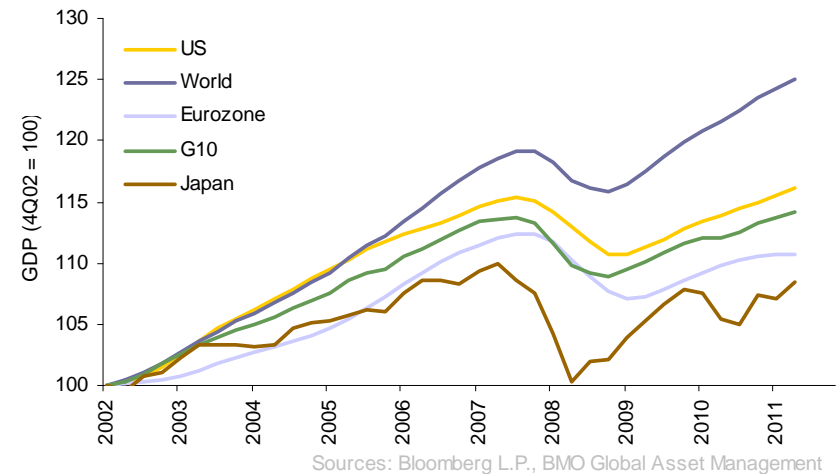


Sources: Bloomberg L.P., BMO Global Asset Management

**European Governments**  
10-yr Bond Yields



**Real GDP**

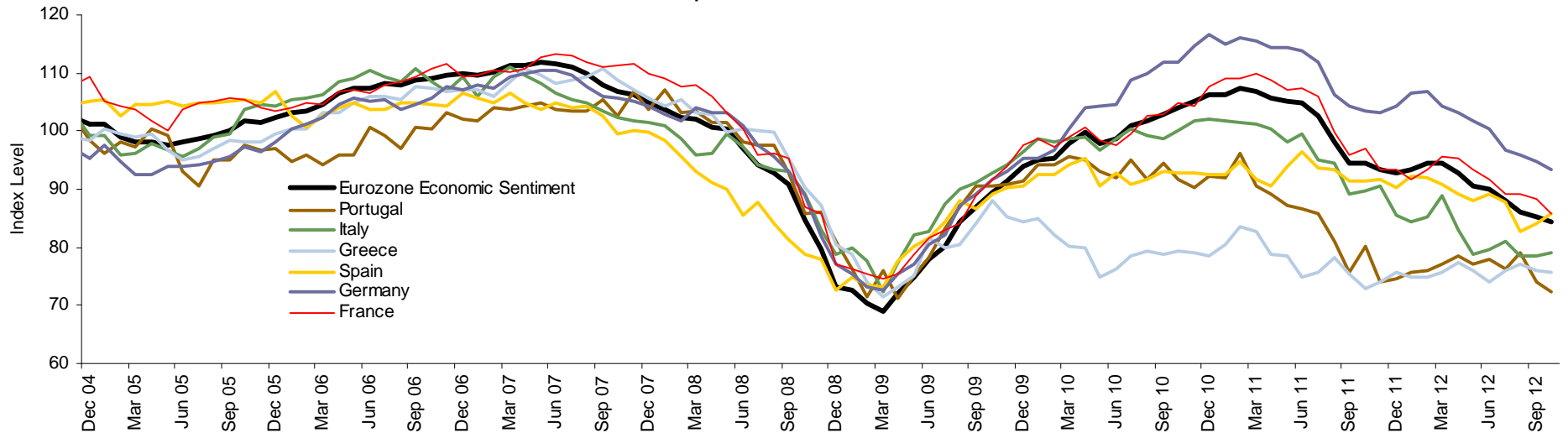


# European Economies

Downward trending sentiment indicators from several European countries have been the norm since late 2010. A declining trend in the European Purchasing Managers Index has been halted, the index remaining relatively flat in the last three months.

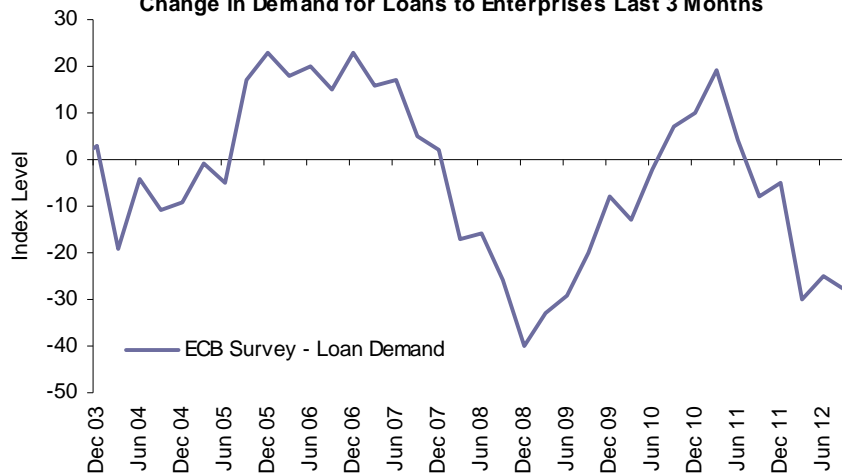
Economy

European Economic Sentiment Indicators



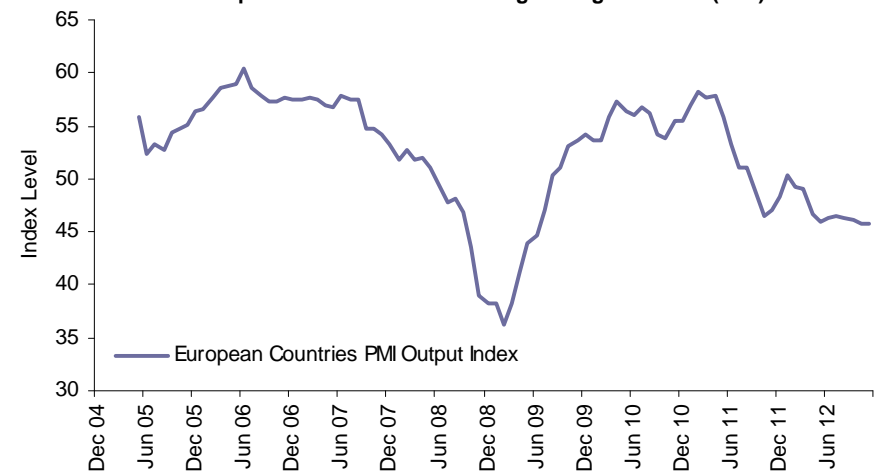
Sources: Bloomberg L.P., BMO Global Asset Management

European Central Bank Survey  
Change in Demand for Loans to Enterprises Last 3 Months



Sources: Bloomberg L.P., BMO Global Asset Management

European Countries Purchasing Managers Index (PMI)



Sources: Bloomberg L.P., BMO Global Asset Management

# BRIC Economies

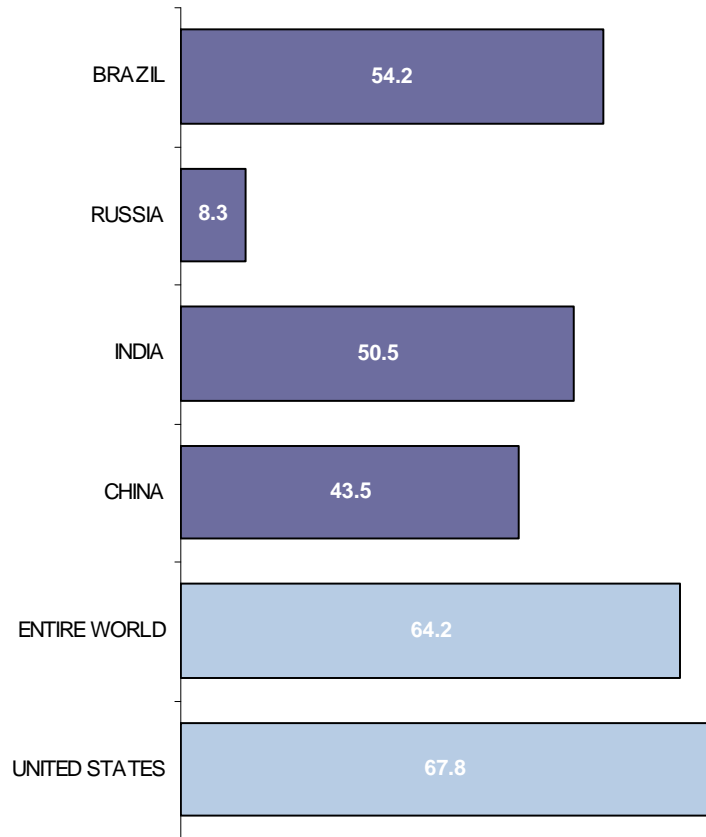
Over the past 10 years, emerging markets economies boomed. China grew by approximately 50%, while other Asian and BRICs economies doubled in size.

As the world economies slow, near term growth prospects are unambiguously much lower.

Economy

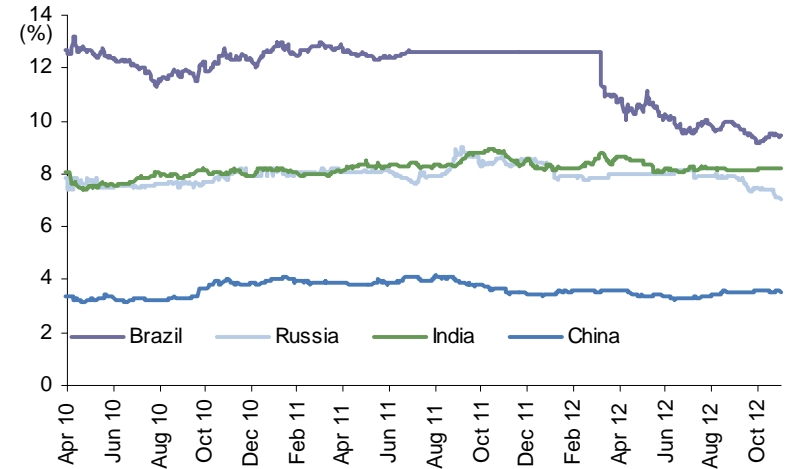
## BRIC Countries

Percentage Debt to GDP by Country on 12/31/2011



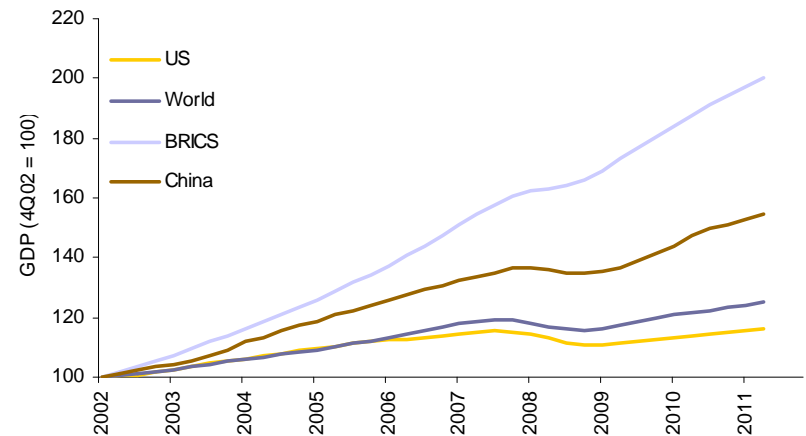
Sources: Bloomberg L.P., BMO Global Asset Management

## BRIC Governments 10-yr Bond Yields



Sources: Bloomberg L.P., BMO Global Asset

## Real GDP



Sources: Bloomberg L.P., BMO Global Asset Management

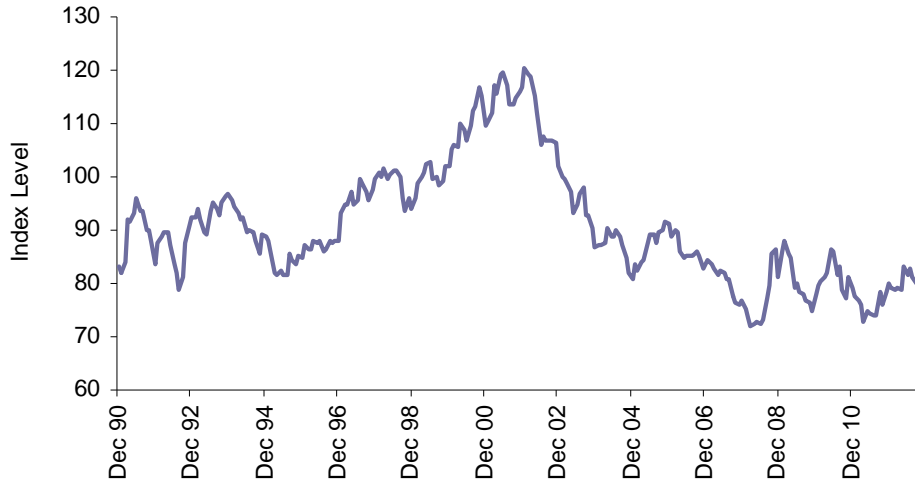


# Currencies

The dollar's relative strength is one factor which explains weak revenue growth in the third quarter. The Fiscal Cliff has the potential to reverse the dollar's recent strength.

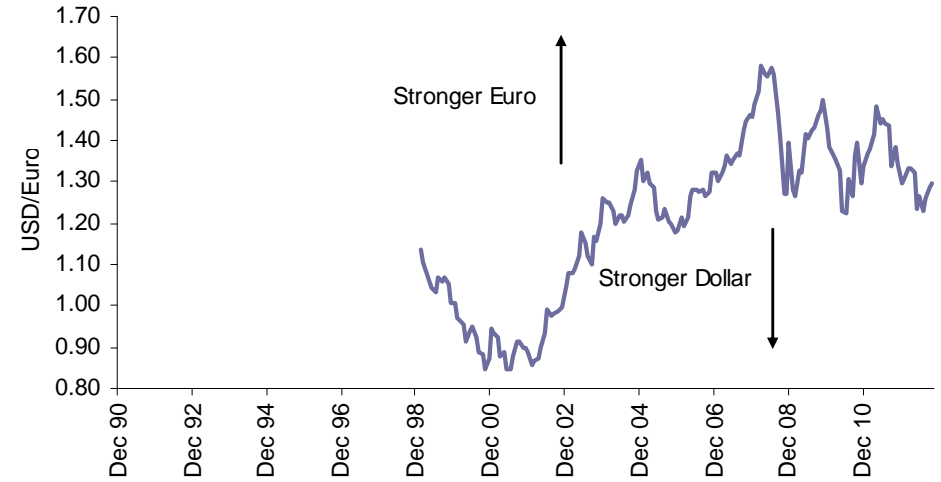
Economy

**U.S. Dollar Strength Relative to a Basket of Currencies**



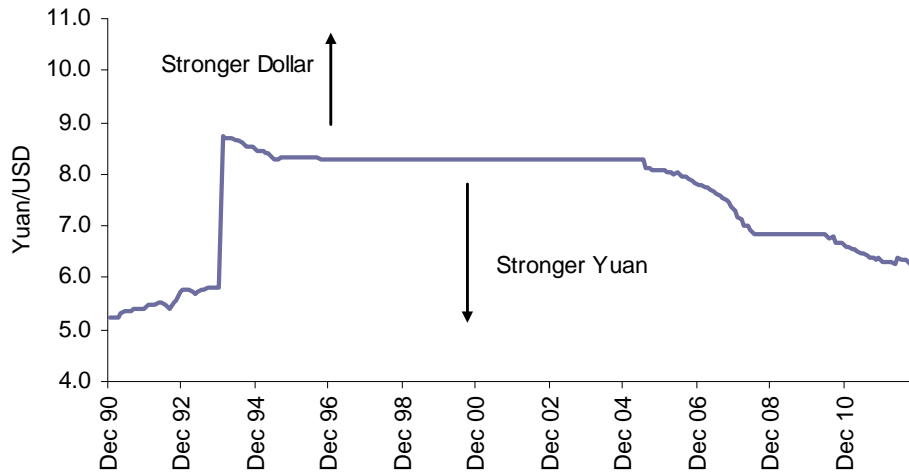
Sources: Bloomberg L.P., BMO Global Asset Management

**U.S. Dollar Strength Relative to Euro**



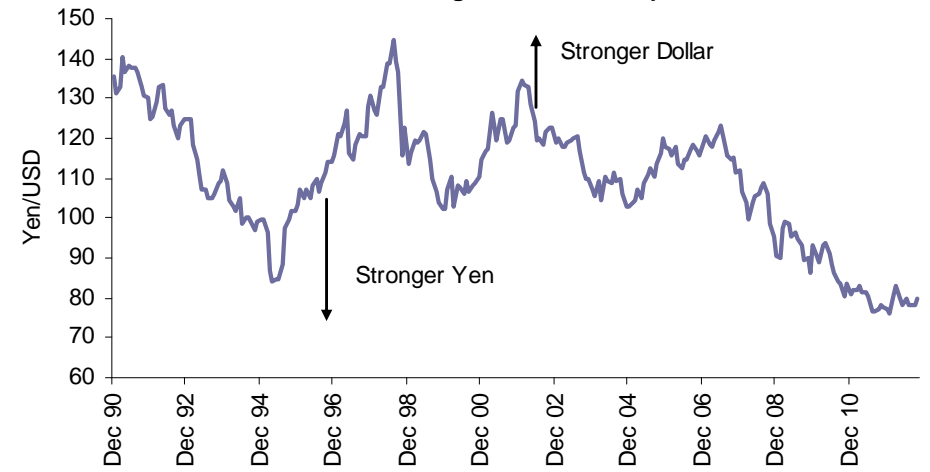
Sources: Bloomberg L.P., BMO Global Asset Management

**U.S. Dollar Strength Relative to Chinese Yuan**



Sources: Bloomberg L.P., BMO Global Asset Management

**U.S. Dollar Strength Relative to Japanese Yen**



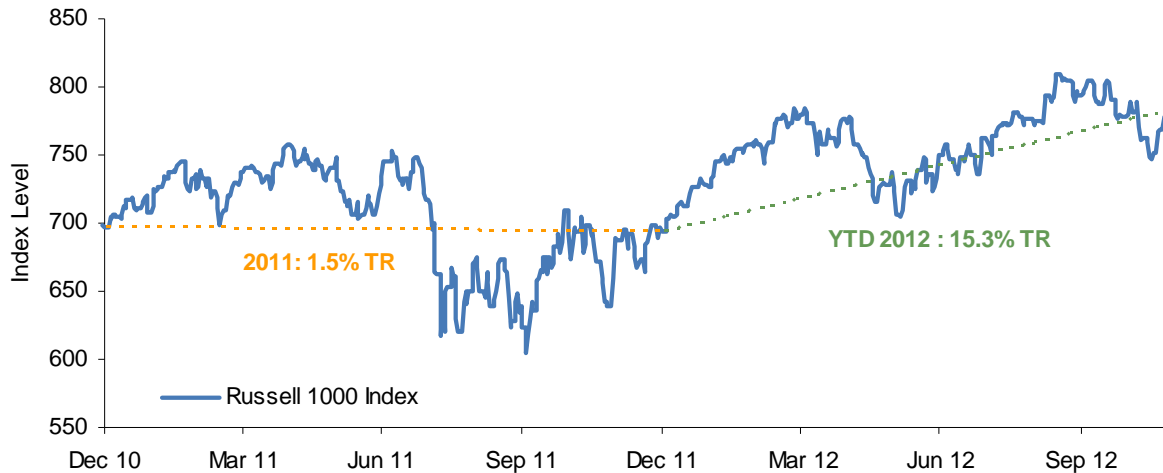
Sources: Bloomberg L.P., BMO Global Asset Management

# Investment Style Performance

All equity styles and market caps posted positive returns YTD.  
Large cap stocks have continued to outperform small cap stocks YTD.

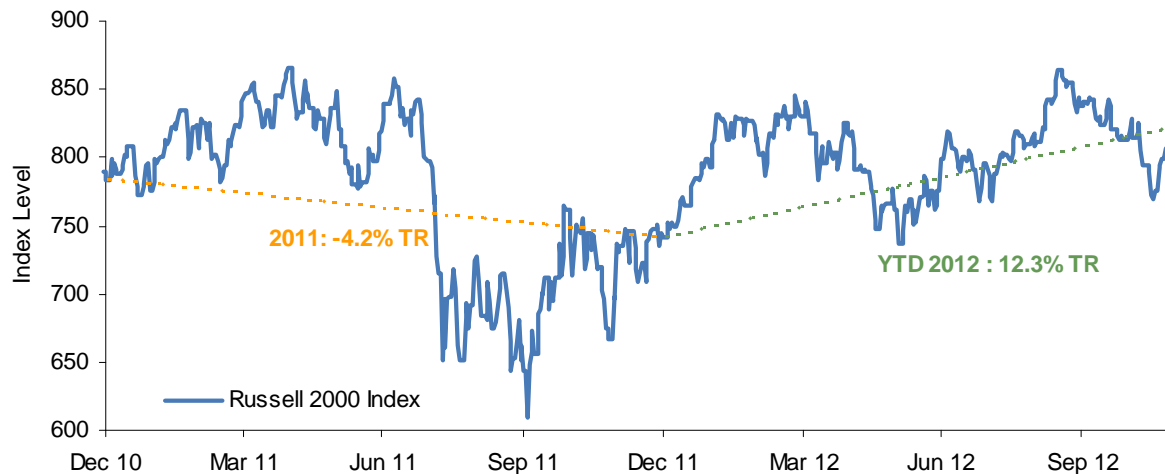
Stocks

Large Cap Stocks



Sources: Bloomberg L.P., BMO Global Asset Management

Small Cap Stocks



Sources: Bloomberg L.P., BMO Global Asset Management

Total Returns (%)

		YTD 11/30/2012		
		Value	Blend	Growth
Market Cap	Large	15.1	15.3	15.3
	Mid	15.5	15.1	13.8
	Small	13.3	12.3	11.4

		2011		
		Value	Blend	Growth
Market Cap	Large	0.4	1.5	2.6
	Mid	-1.4	-1.5	-1.7
	Small	-5.5	-4.2	-2.9

Total returns are based on Russell-style indices performance and include dividends. Graphs depict price levels only. Sources: Bloomberg L.P., BMO Global Asset Management.

# Investment Style Performance

Indices across styles and sizes have doubled their levels since their post-crisis lows. Large and small cap have both approached their previous highs.

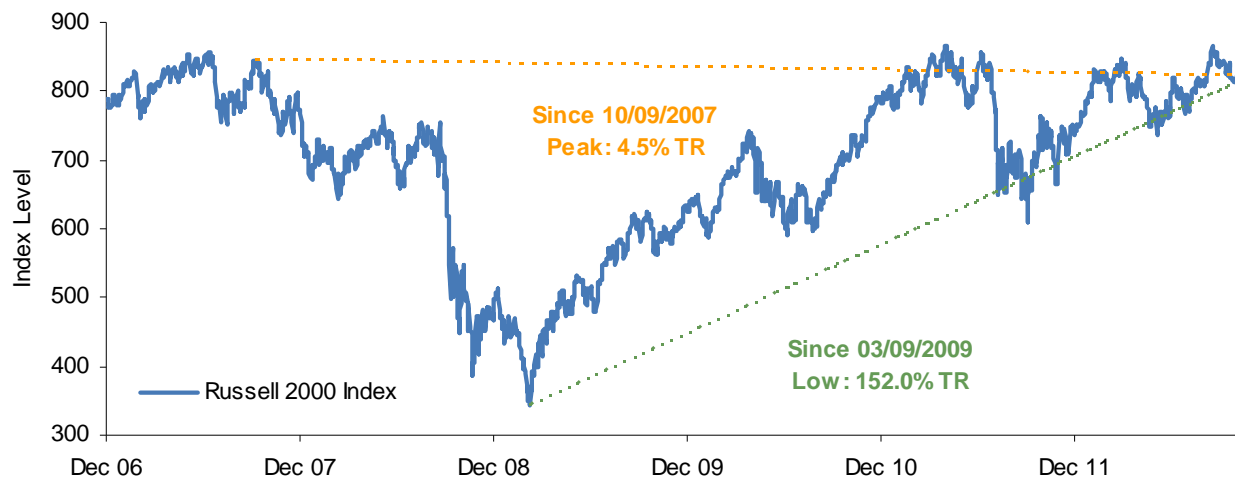
Stocks

## Large Cap Stocks



Sources: Bloomberg L.P., BMO Global Asset Management

## Small Cap Stocks



Sources: Bloomberg L.P., BMO Global Asset Management

## Total Returns (%)

As of 11/30/2012

### Since Peak 10/9/2007

	Value	Blend	Grow th
Large	-7.4	2.7	12.7
Mid	7.2	9.5	9.6
Small	1.4	4.5	7.0

### Since Low 3/9/2009

	Value	Blend	Grow th
Large	130.9	130.3	129.9
Mid	173.6	164.2	153.5
Small	150.7	152.0	152.6

Total returns are based on Russell-style indices performance and include dividends. Total returns are cumulative returns for the period, not annualized. Peak market date is 10/09/2007. Low market date is 03/09/2009. Graphs depict price levels only. Sources: Bloomberg L.P., BMO Global Asset Management.

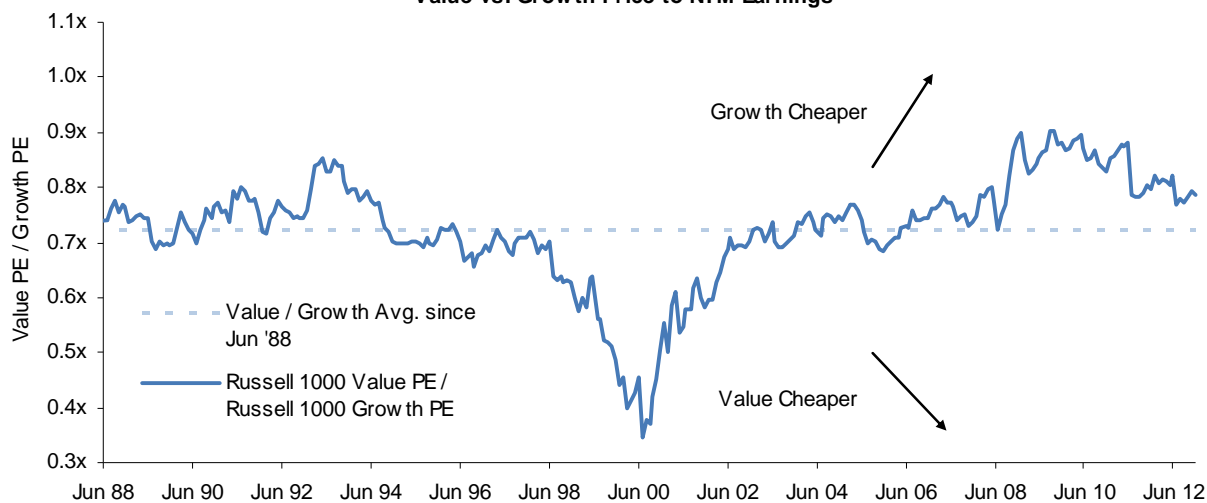
# Investment Style Valuations

Current multiples of U.S. small cap companies are near their historical norms, but appear elevated relative to large cap companies' P/Es.

Growth stocks appear cheap across the market cap spectrum.

Stocks

Value vs. Growth Price to NTM Earnings



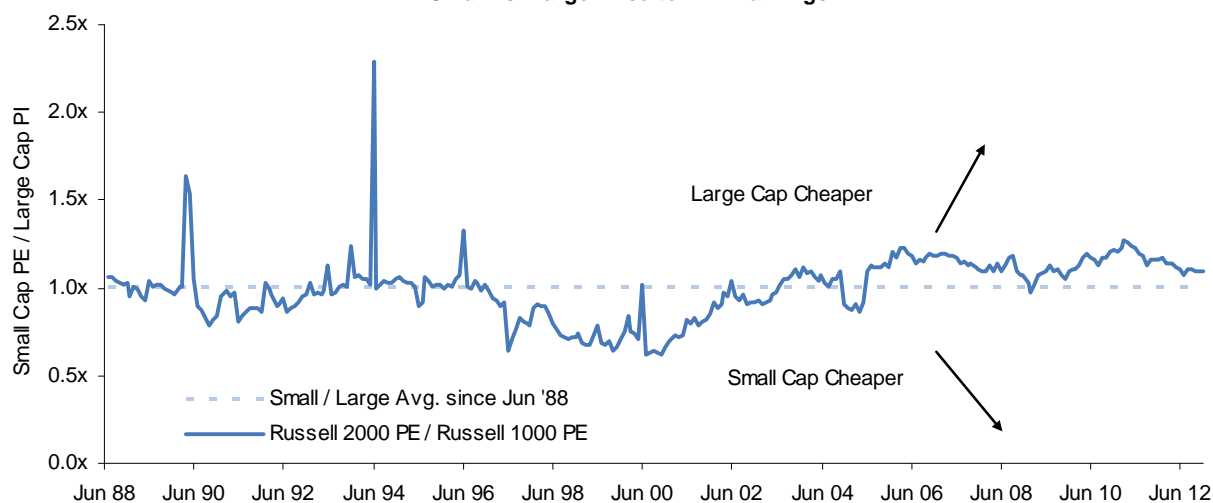
Sources: FactSet, BMO Global Asset Management

P/E vs. Long Term Average\*

As of 11/30/2012

Current P/E (Avg. P/E)	Value	Blend	Growth
Large	<b>11.5</b> (13.5)	<b>12.9</b> (16.0)	<b>14.7</b> (19.8)
Mid	<b>12.9</b> (13.6)	<b>14.2</b> (15.5)	<b>16.1</b> (19.6)
Small	<b>13.1</b> (13.6)	<b>14.1</b> (15.4)	<b>15.4</b> (18.0)

Small vs. Large Price to NTM Earnings



Sources: FactSet, BMO Global Asset Management

Current PE as % of Avg PE	Value	Blend	Growth
Large	<b>85.6%</b>	<b>80.8%</b>	<b>74.1%</b>
Mid	<b>94.6%</b>	<b>91.6%</b>	<b>82.2%</b>
Small	<b>96.4%</b>	<b>91.5%</b>	<b>85.8%</b>

\*Data begins in June 1988. Data based on Russell-style indices. Earnings are estimated earnings for the next 12 months (NTM). Sources: FactSet, BMO Global Asset Management.

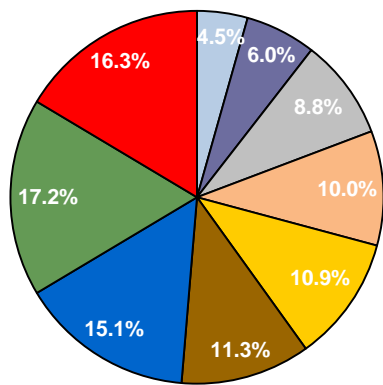
# Sector Performance

The Consumer Discretionary sector was the top performer in the large cap category and the Material sector was the leader in the small cap category through the end of November 2012. The Energy sector was the laggard in 2012 through the end of November.

Stocks

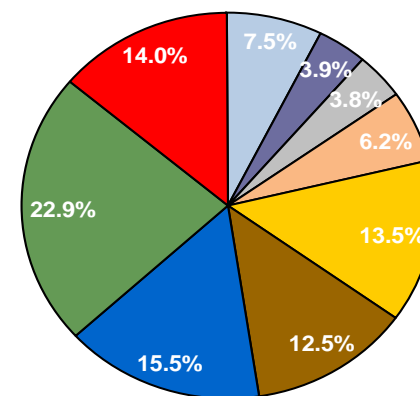
As of 11/30/2012		Russell Index	Materials and Processing	Utilities	Consumer Staples	Energy	Producer Durables	Health Care	Consumer Discretionary	Financials	Technology
LARGE CAP EQUITIES	YTD 2012	15.3%	14.1%	8.2%	12.6%	3.4%	13.4%	19.9%	24.9%	22.5%	12.4%
	MTD	0.8%	2.1%	-2.7%	2.4%	-1.2%	1.9%	1.0%	2.7%	-0.1%	0.9%
	2011	1.5%	-6.9%	12.6%	14.5%	3.5%	-1.9%	11.8%	5.5%	-12.9%	0.3%
SMALL CAP EQUITIES	YTD 2012	12.3%	21.9%	3.6%	10.2%	-8.2%	10.5%	16.1%	20.6%	17.3%	4.8%
	MTD	0.5%	1.9%	-3.2%	0.8%	-1.2%	1.3%	0.7%	2.3%	-0.6%	1.6%
	2011	-4.2%	-8.9%	10.5%	5.0%	-6.4%	-6.1%	2.2%	-7.2%	-2.9%	-8.4%

Russell 1000 Index Composition



- Materials and Processing
- Utilities
- Consumer Staples
- Energy
- Producer Durables
- Health Care
- Consumer Discretionary
- Financials
- Technology

Russell 2000 Index Composition



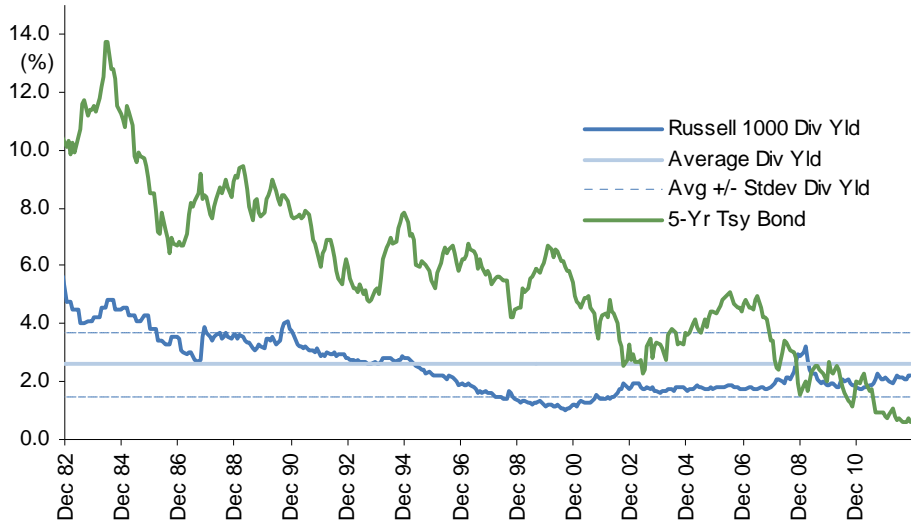
Sources: Bloomberg L.P., BMO Global Asset Management . Sector break-down based on Russell categories.

# Other Stock Valuations and Metrics

Stocks offer an attractive dividend yield when compared to the shorter Treasury bonds. The estimated EPS for 2012 translates into an 5.7% growth in earnings. At its 2012 peak, the estimated growth in earnings was 10.2%. Revenue per share for 3Q2012 was 4% below expectations.

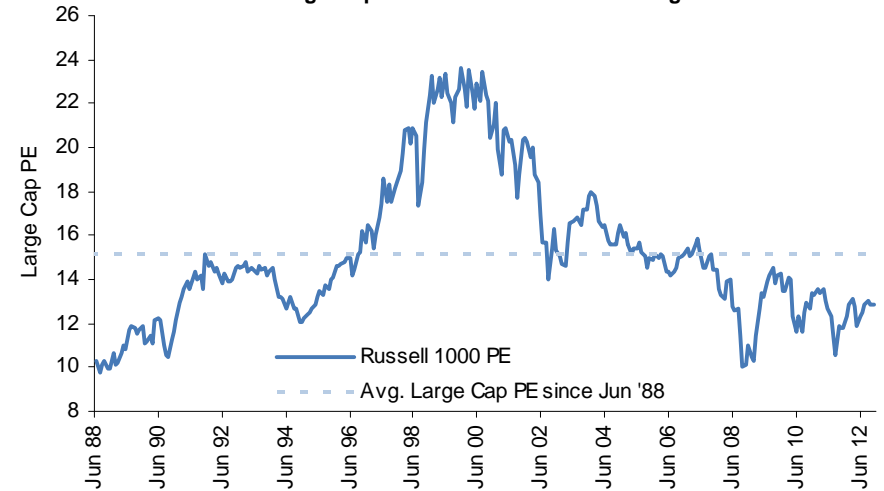
Stocks

Dividend Yield



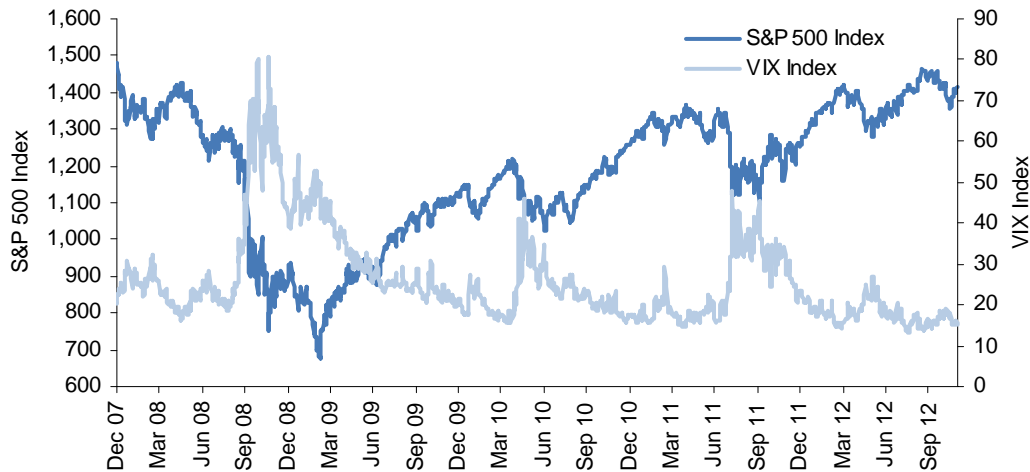
Sources: FactSet, Bloomberg L.P., BMO Global Asset Management

U.S. Large Cap Stocks Price to NTM Earnings



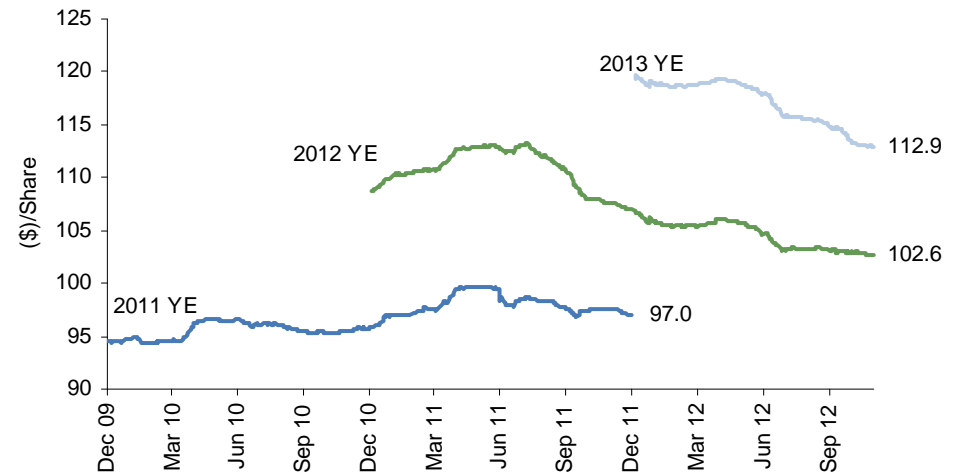
Sources: FactSet, BMO Global Asset Management

Implied Stock Market Volatility and the S&P 500 Index



Sources: Bloomberg L.P., BMO Global Asset Management

Year-End Consensus EPS Estimate for the S&P500 Index



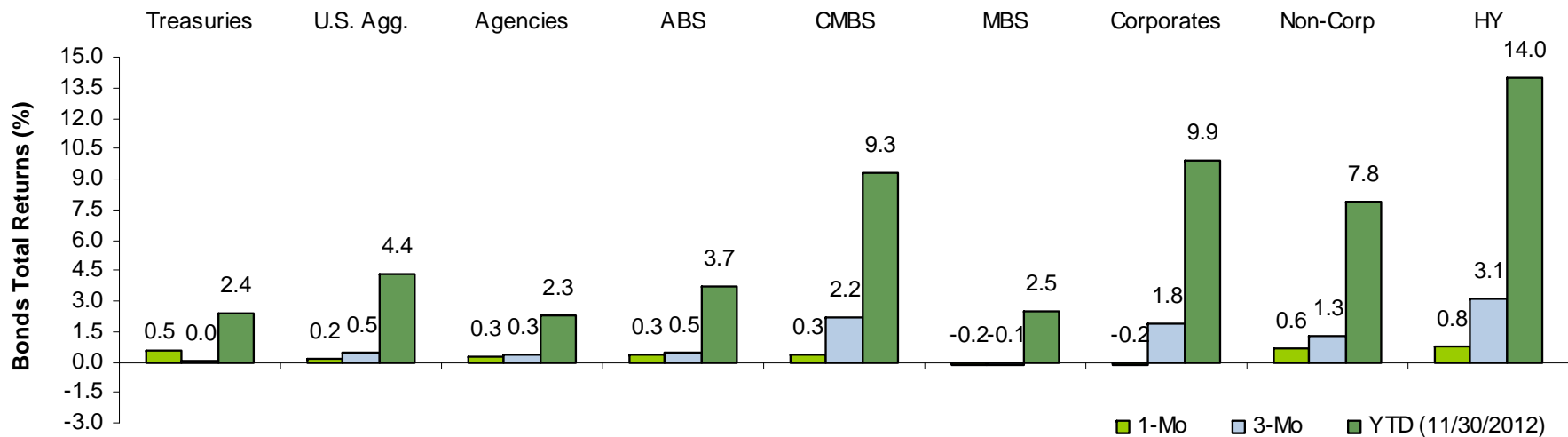
Sources: FactSet, BMO Global Asset Management



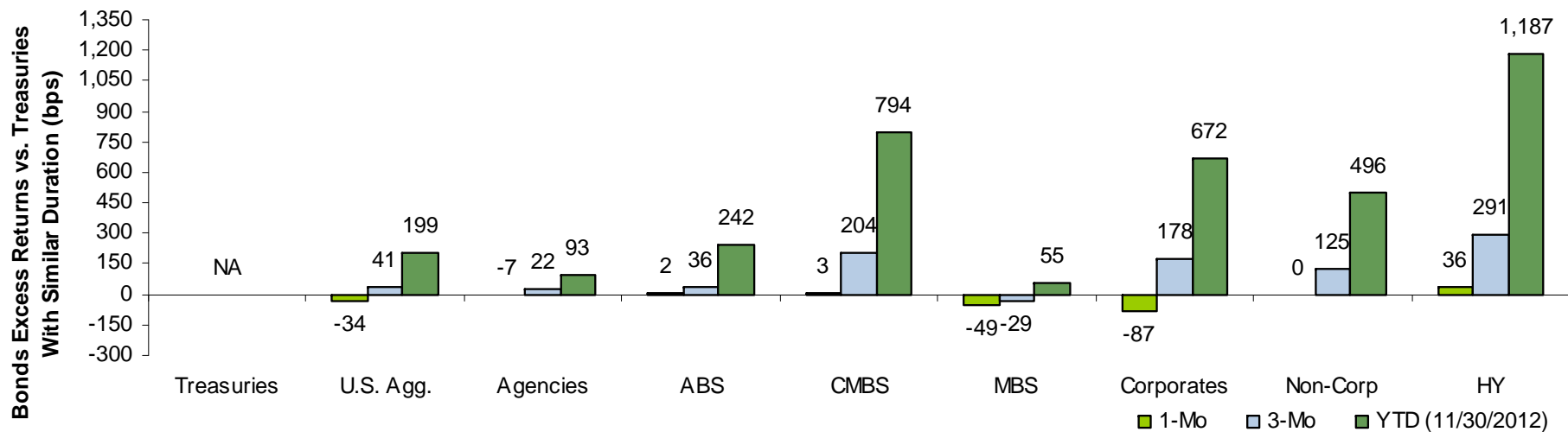
# U.S. Bond Market Performance

All bond sectors have posted positive returns in 2012. Despite renewed Eurozone recession concerns, credit sectors posted strong returns and High Yield leads with 14.0% YTD.

Bonds



Sources: Barclays Capital, BMO Global Asset Management

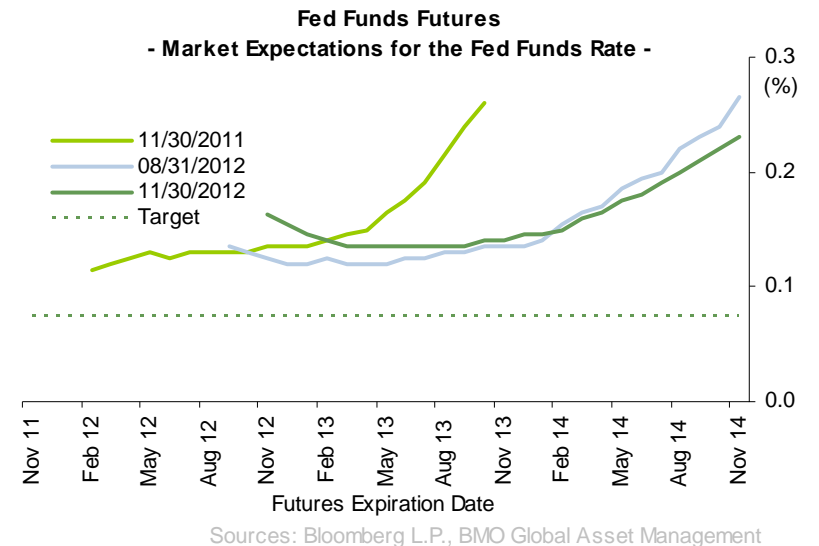
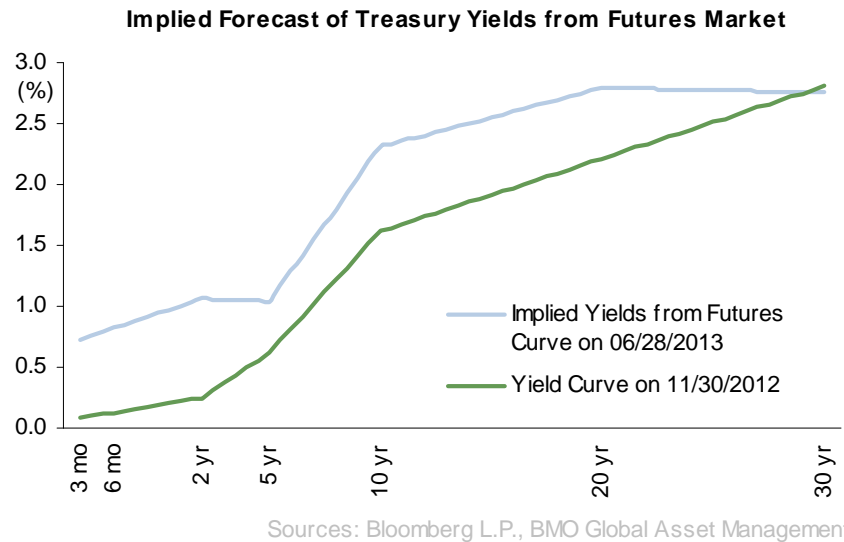
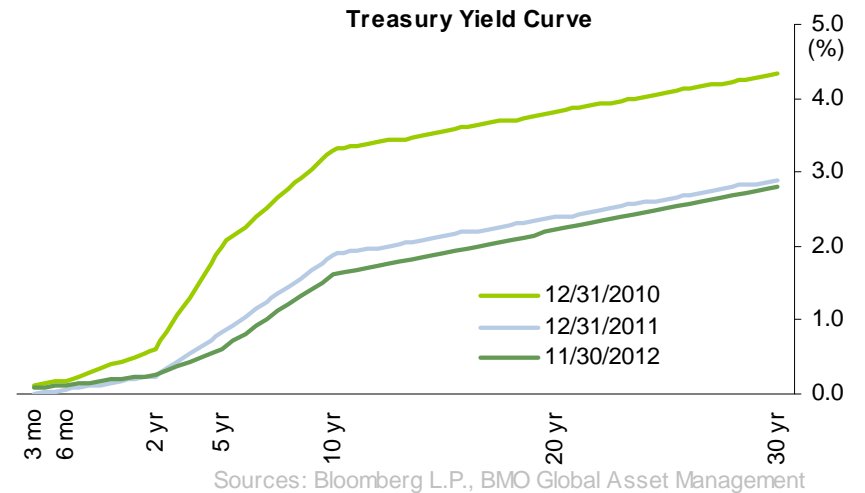
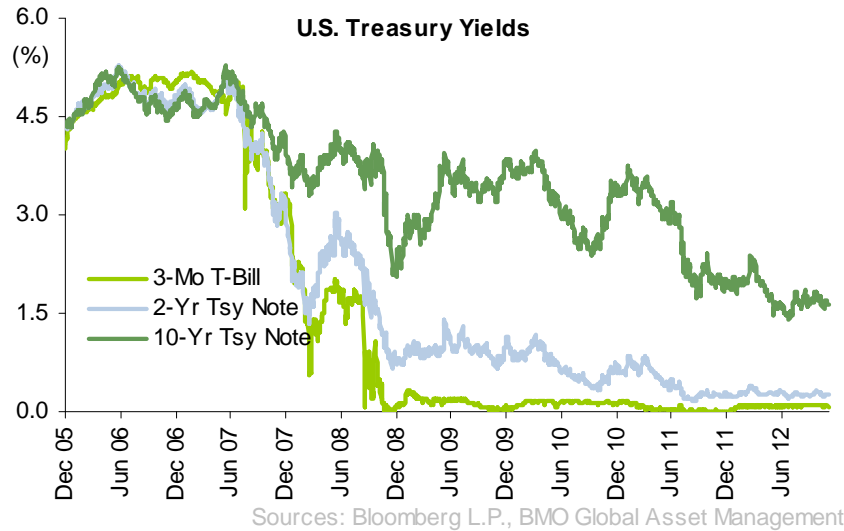


Sources: Barclays Capital, BMO Global Asset Management

# U.S. Treasury Yields

In 2012, yields have decreased modestly across the yield curve, reaching historical lows. Fed Funds rate expectations have fallen further, as the Fed expects to maintain low rates "at least through mid-2015."

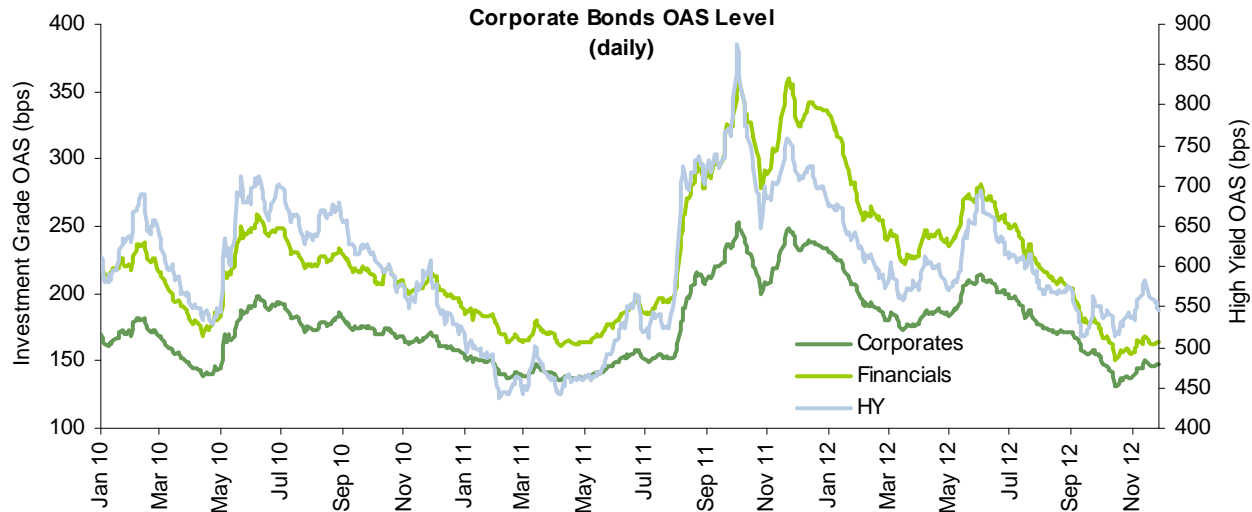
Bonds



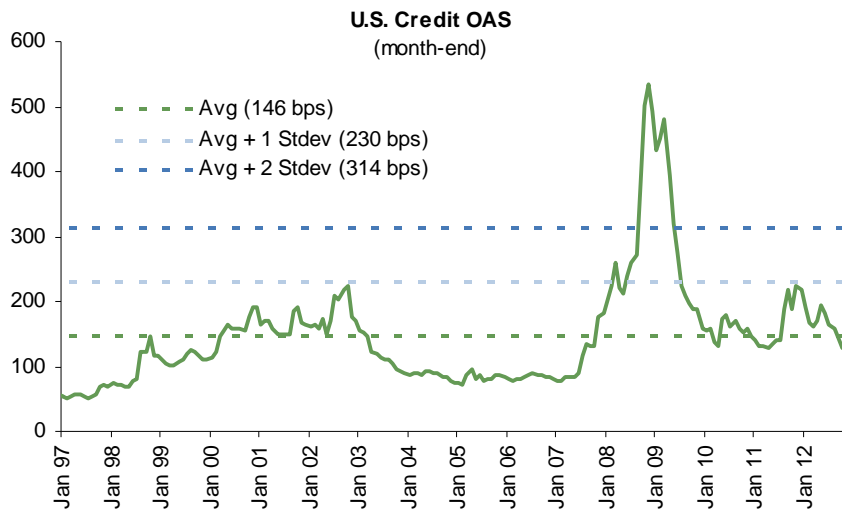
# Bond Spreads

Corporate spreads have been on a declining path since end of May through mid-October, as investors searched for yields. Although spreads have widened since their 2012 lows reached around mid-October, they remain slightly below the long-term average.

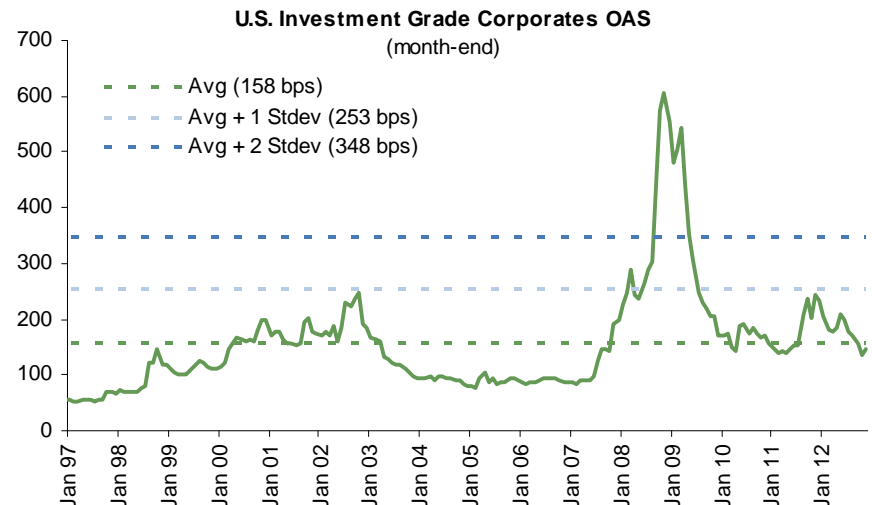
Bonds



Sources: Barclays Capital, BMO Global Asset Management



Source: Barclays Capital, BMO Global Asset Management



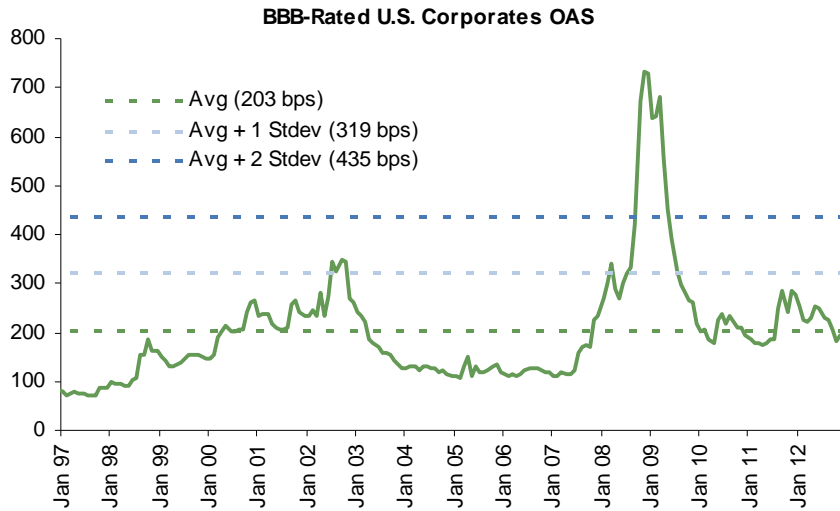
Source: Barclays Capital, BMO Global Asset Management

The average and standard deviation are calculated using monthly data starting January 1997.

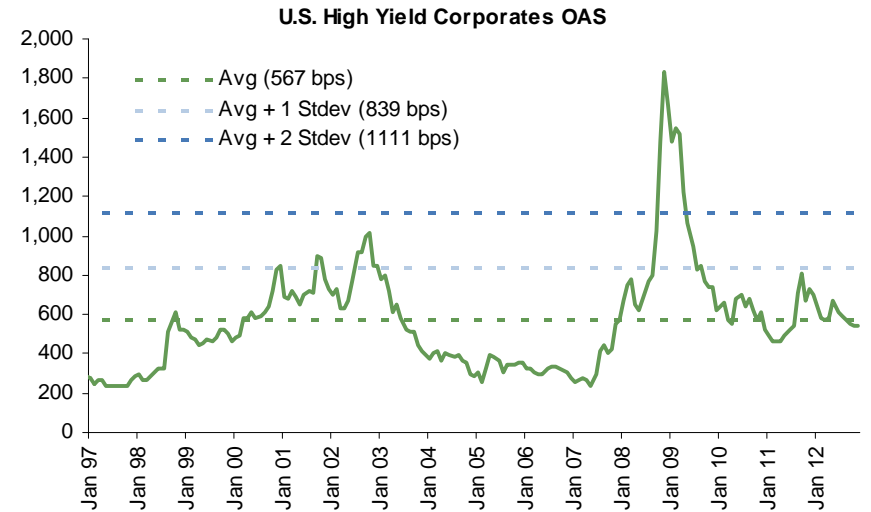
# Bond Spreads

Emerging market spreads on government and corporate debt remained relatively flat in November, landing below their long-term average.

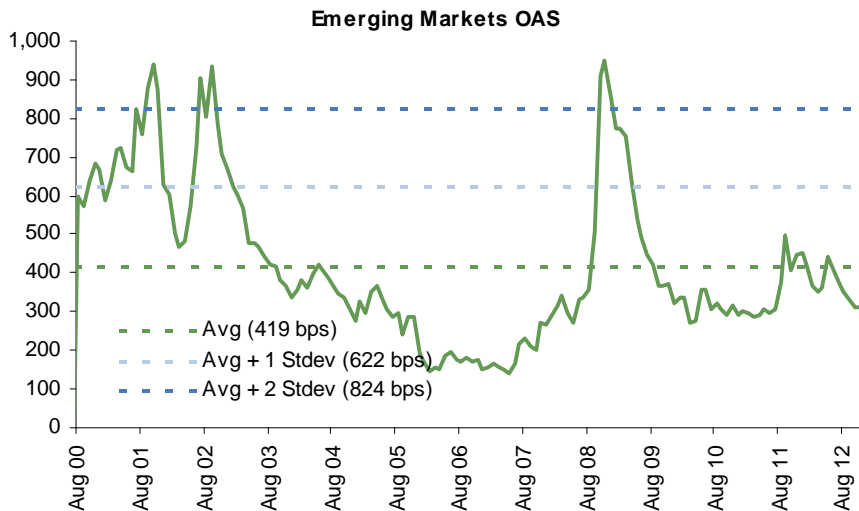
Bonds



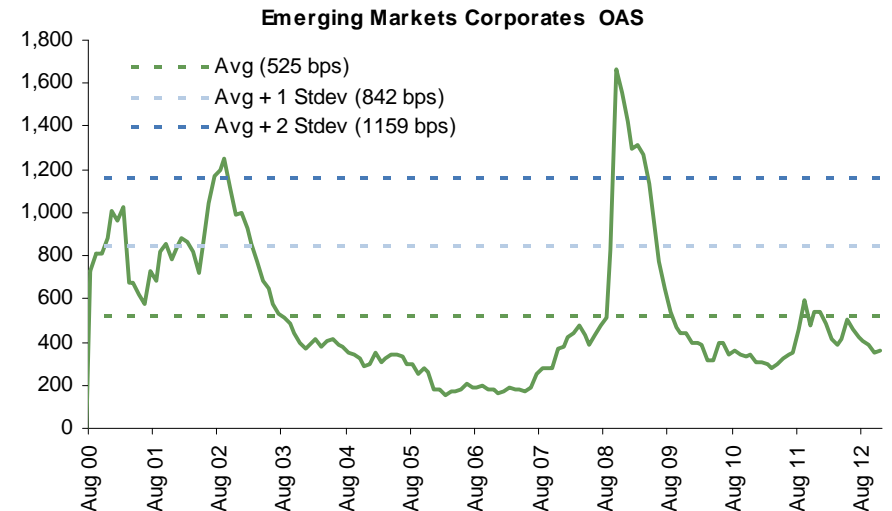
Source: Barclays Capital, BMO Global Asset Management



Source: Barclays Capital, BMO Global Asset Management



Source: Barclays Capital, BMO Global Asset Management



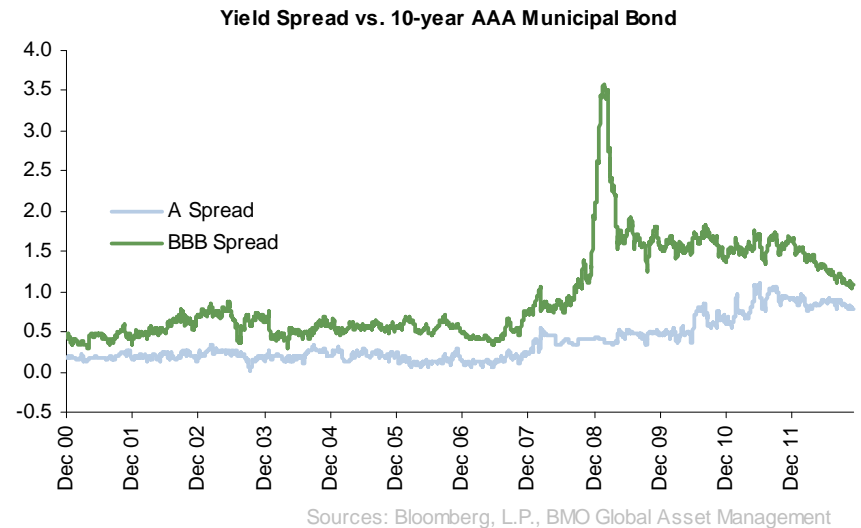
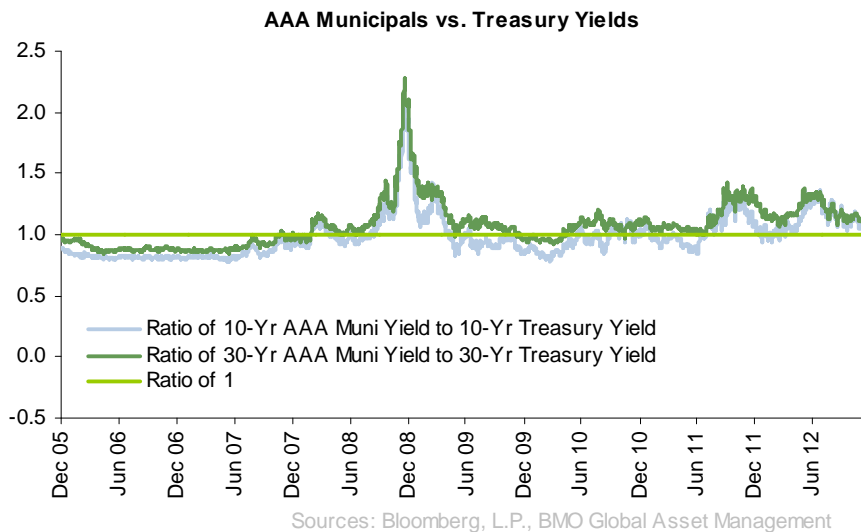
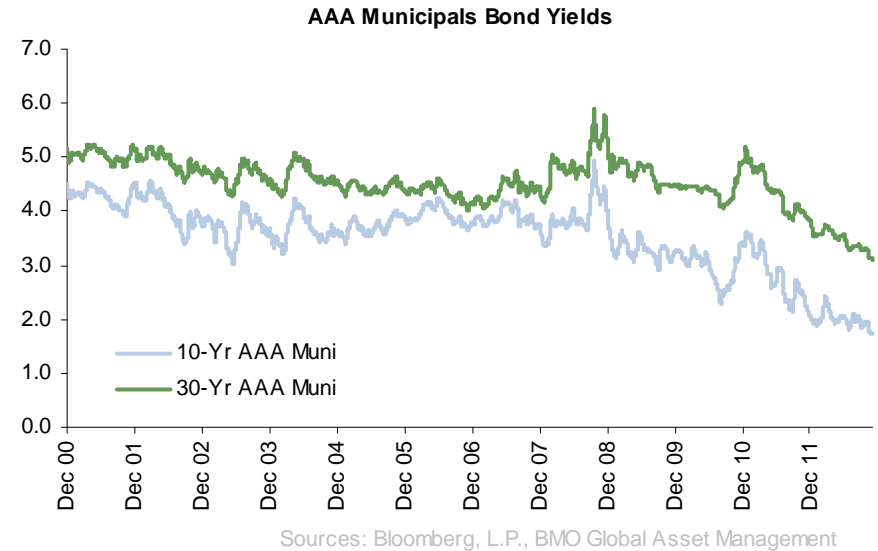
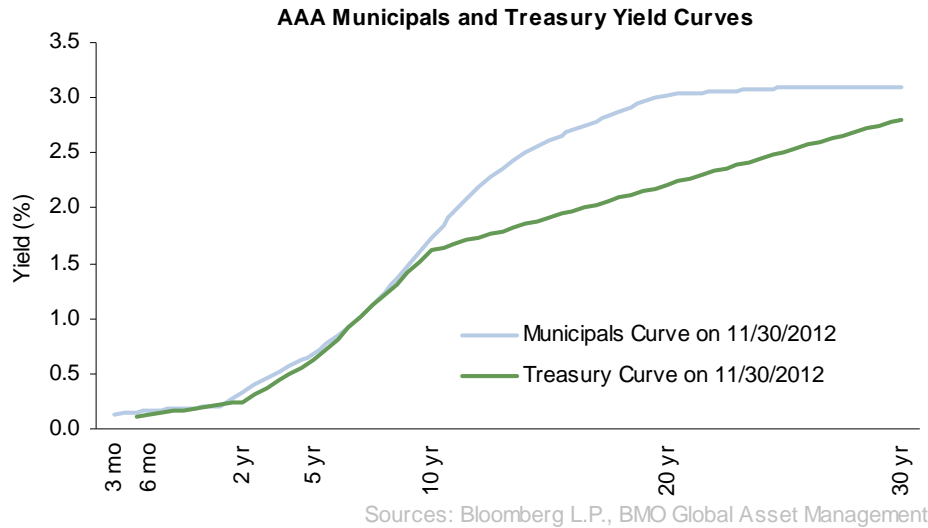
Source: Barclays Capital, BMO Global Asset Management

The average and standard deviation are calculated using monthly data starting in January 1997 for the U.S. series, and starting in August 2000 for the Emerging Markets series.

# Municipal Bonds

Longer-maturity AAA-rated Municipals bonds carry a higher yield than Treasury securities with similar maturities. In addition, investors get a healthy yield pick-up by moving down the quality spectrum.

Bonds



# Bond Market Snapshot

Bonds

11/30/2012	U.S. Aggregate	U.S. Treasury	1-10 yr Municipals	Inv. Grade Corporates	Finance	Industrial	MBS	High Yield	Emerging Markets (EM)	EM Corporates
MTD Total Return	0.16	0.52	0.91	-0.16	0.40	-0.44	-0.17	0.80	1.03	-0.08
3-Mo Total Return	0.49	0.04	1.58	1.84	2.99	1.29	-0.13	3.10	3.90	3.85
YTD Total Return	4.36	2.44	4.36	9.89	14.39	7.70	2.45	14.02	16.78	16.15
12-Mo Total Return	5.51	3.43	5.93	12.24	16.55	10.24	3.17	17.05	18.46	17.41
MTD Excess Return	-0.34	NA	NA	-0.87	-0.17	-1.20	-0.49	0.36	0.26	-0.77
3-Mo Excess Return	0.41	NA	NA	1.78	2.88	1.25	-0.29	2.91	3.68	3.60
YTD Excess Return	1.99	NA	NA	6.72	11.79	4.30	0.55	11.87	13.20	12.95
12-Mo Excess Return	2.30	NA	NA	7.89	13.08	5.55	0.72	14.23	13.65	13.14
Yield to Maturity	1.69	0.81	NA	2.69	2.59	2.68	2.15	7.03	4.47	4.88
OAS	57	NA	NA	147	163	138	58	546	311	364
Average* OAS (since Jan 1997)	66	NA	NA	158	168	153	61	567	419	525
Stdev* of OAS (since Jan 1997)	36	NA	NA	95	132	76	30	272	202	317
Duration (Mod. Adj.)	5.00	5.55	4.12	7.22	5.71	7.71	2.79	4.15	6.82	6.02
Maturity (years)	6.92	6.73	6.11	10.60	7.85	11.50	4.44	6.73	11.07	8.82
Coupon	3.60	2.23	4.82	4.98	4.99	4.88	4.36	7.92	6.73	6.30
Price	109.63	108.12	114.03	114.42	112.20	114.91	107.90	103.48	113.98	107.77
Market Value (\$ millions)	16,948,414	6,157,712	669,056	3,651,206	1,185,026	2,063,445	4,989,259	1,124,537	845,642	185,970
Quality	AA1/AA2	AAA/AAA	AA2/AA3	A3/BAA1	A2/A3	A3/BAA1	AAA/AAA	B1/B2	BAA3/BA1	BAA3/BA1

\* The average OAS and standard deviation of OAS for Emerging Markets indices are based on monthly data starting in August 2000.

Sources: Barclays Capital, BMO Global Asset Management



# Commodities

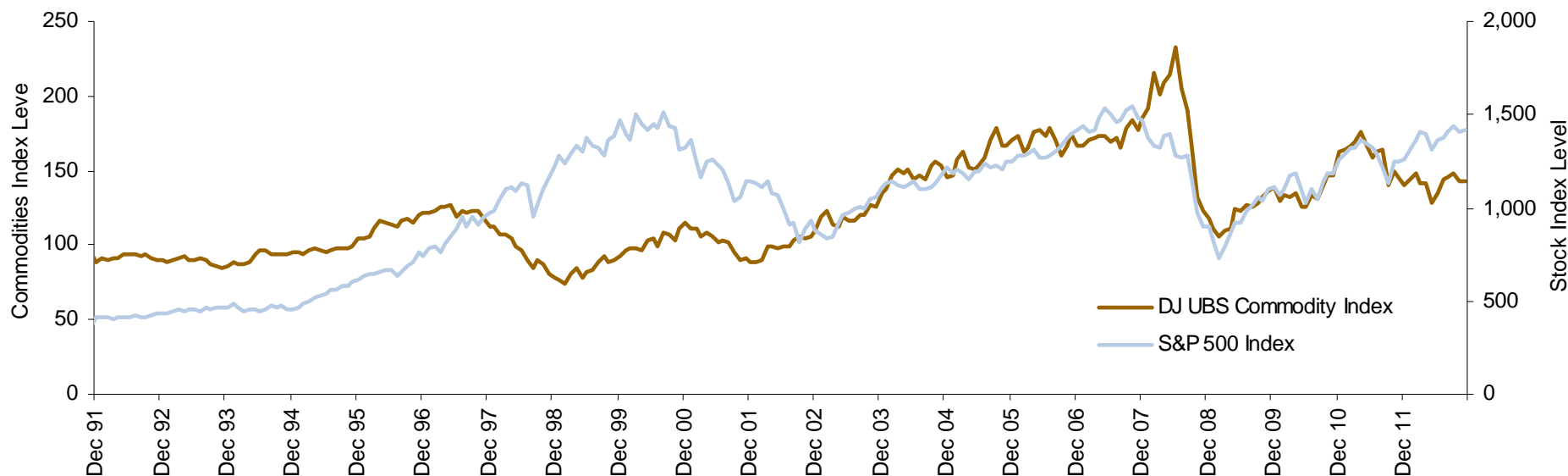
Commodities have seen increased correlation to equity prices since the onset of the last credit crisis, but a short-lived decoupling can be observed at the beginning of 2012.

Alternative Assets

As of 11/30/2012	DJ UBS Agriculture Subindex	DJ UBS Livestock Subindex	DJ UBS Grains Subindex	DJ UBS Energy Subindex	DJ UBS Precious Metals Subindex	DJ UBS Industrial Metals Subindex	DJ UBS Commodity Index	S&P 500 Index
MTD	-2.8	1.5	-3.5	-1.1	-9.3	7.0	0.1	0.6
YTD	8.7	-4.1	25.8	-7.6	-11.7	1.3	1.6	15.0
2011	-14.4	-2.4	-14.5	-16.0	-18.5	-24.3	-13.3	2.1

Sources: Bloomberg L.P., BMO Global Asset Management

Commodities and Stocks



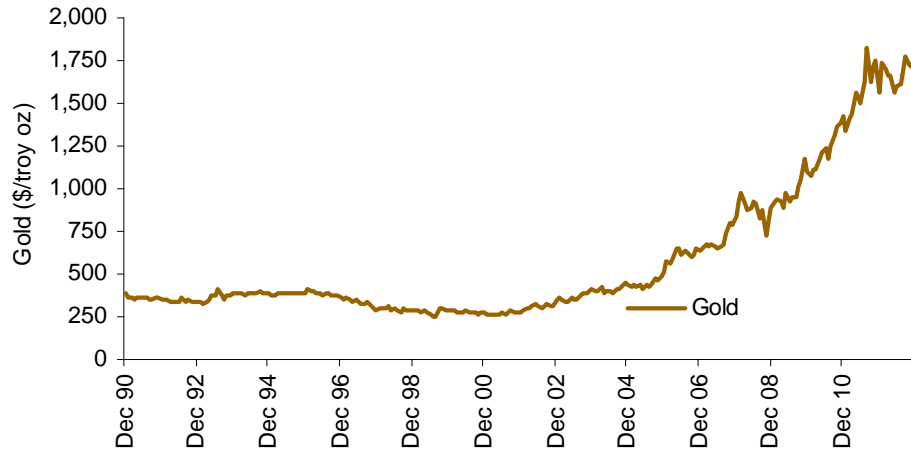
Sources: Bloomberg L.P., BMO Global Asset Management

# Commodities

Most major commodity groups have posted positive returns year to date. Oil prices are the exception. The effect of the summer drought is evident in grain returns.

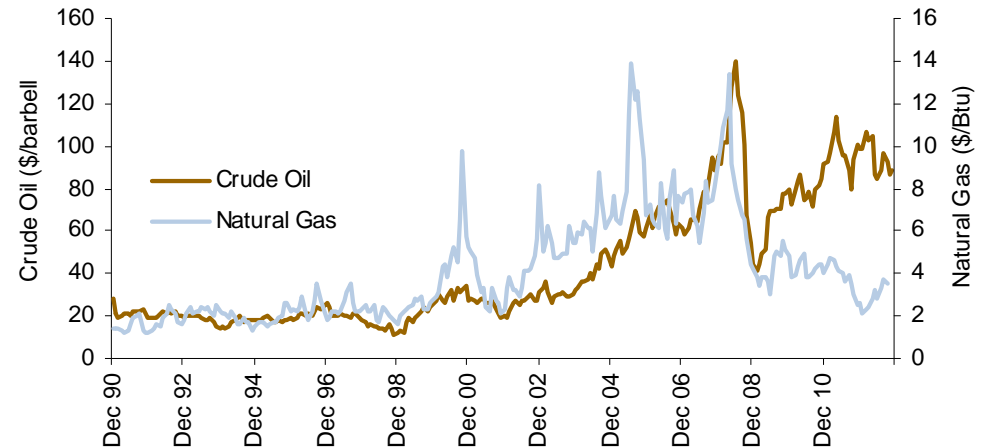
Alternative Assets

Price of Gold



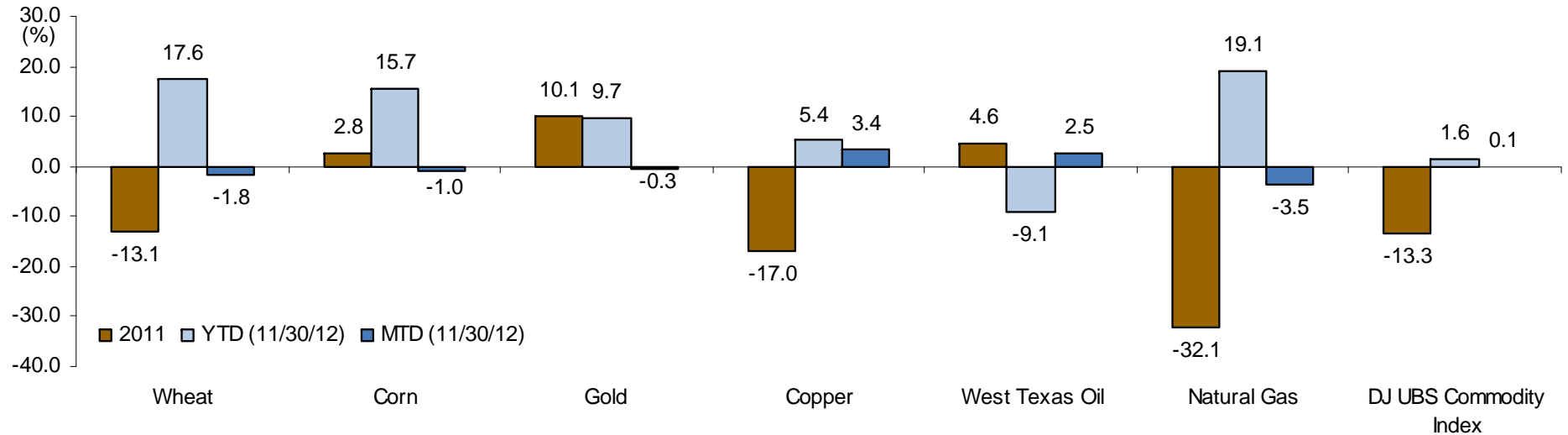
Sources: Bloomberg L.P., BMO Global Asset

Crude Oil and Natural Gas Prices



Sources: Bloomberg L.P., BMO Global Asset Management

Commodities Total Return



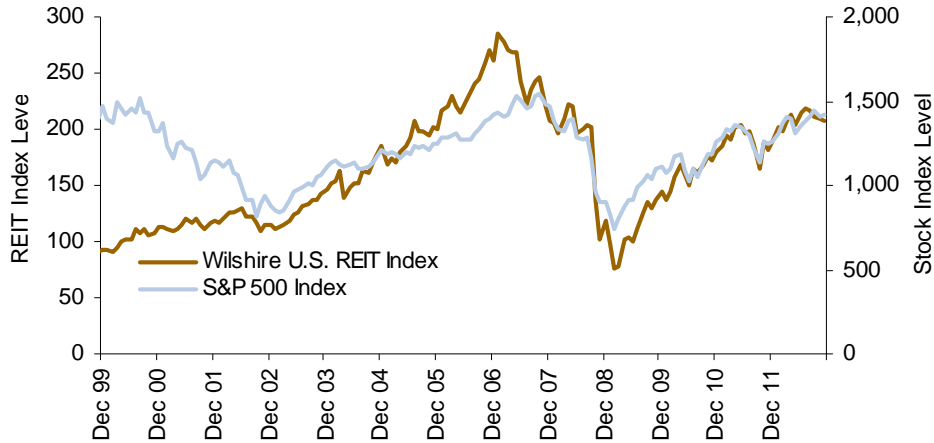
Sources: Bloomberg L.P., BMO Global Asset Management

# Other Alternative Assets

U.S. REITs have underperformed the large cap equities year to date, while global REITs have outperformed.

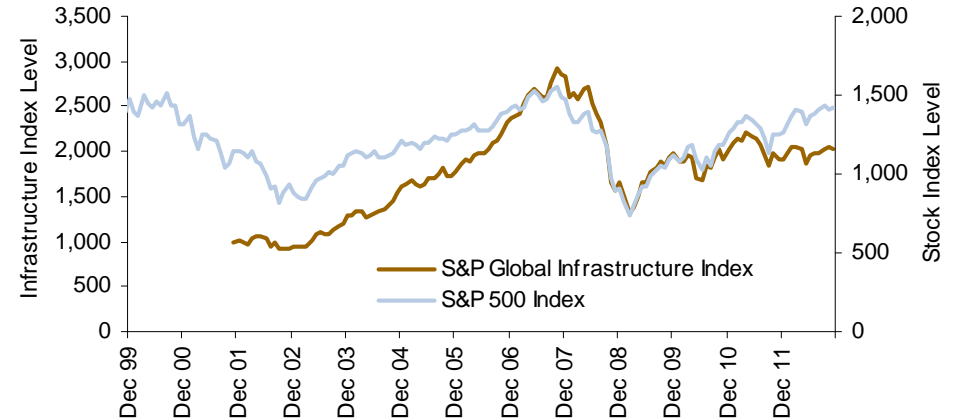
Alternative Assets

REITS and Stocks



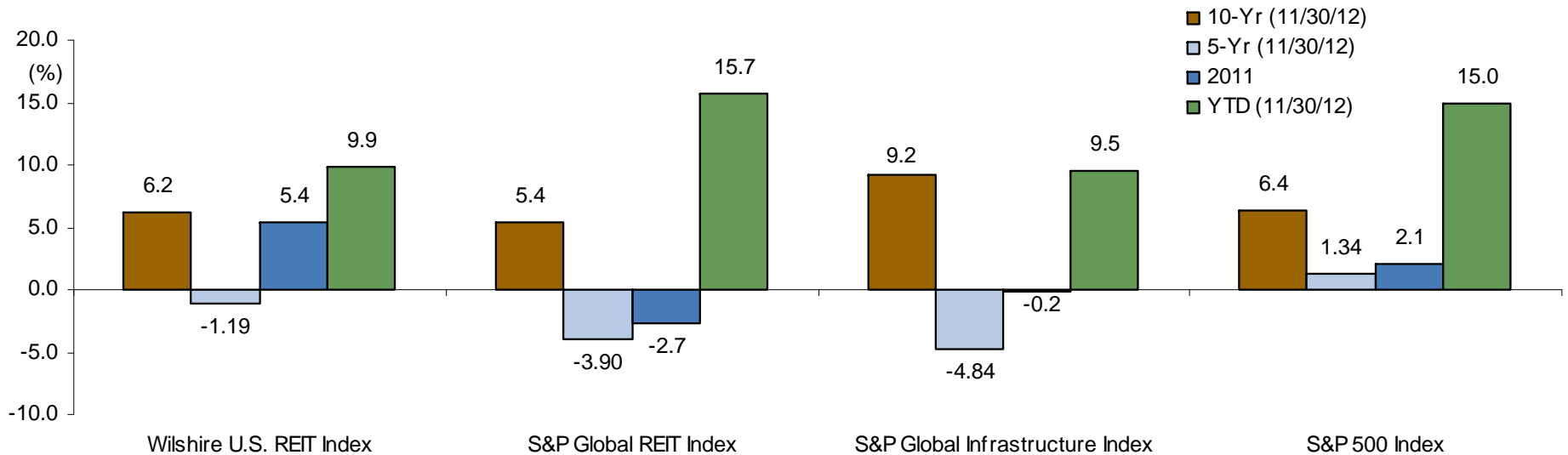
Sources: Bloomberg L.P., BMO Global Asset Management

Global Infrastructure and Stocks



Sources: Bloomberg L.P., BMO Global Asset Management

Alternatives Total Return



Sources: Bloomberg L.P., BMO Global Asset Management

Total returns for periods of one year or more are annualized.

# Investment Strategy Group

Dan Sido	Chief Administrative Officer
Sandy Lincoln	Chief Market Strategist
Bob Decker, CFA	Director, Quantitative Strategies
Irina Pacheco, CFA	Vice President, Quantitative Strategies

# Index Definitions

## Equity Indices

### S&P 500 Index

S&P 500® Index is an unmanaged index of large-cap common stocks.

### Dow Jones Industrial Average

The Dow Jones Industrial Average is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and the Nasdaq.

### Russell 1000 Index

Russell 1000® Index consists of approximately 1,000 of the largest companies in the U.S. equity markets.

### Russell 1000 Growth Index

Russell 1000® Growth Index measures the performance of those Russell 1000 Companies with higher price-to-book ratios and higher forecasted growth values.

### Russell 1000 Value Index

Russell 1000® Value Index measures the performance of those Russell 1000 Companies with lower price-to-book ratios and lower forecasted growth values.

### Russell Midcap Index

Russell Midcap® Index measures the performance of the smallest 800 U.S. companies in the Russell 1000 Index.

### Russell Midcap Growth Index

Russell Midcap® Growth Index measures the performance of those Russell Midcap companies with higher price-to-book ratios and higher forecasted growth values.

### Russell Midcap Value Index

Russell Midcap® Value Index measures the performance of those Russell Midcap companies with lower price-to-book ratios and lower forecasted growth values.

### Russell 2500 Index

The Russell 2500™ Index measures the performance of the small to mid-cap segment of the U.S. equity universe. It is a subset of the Russell 3000® Index.

### Russell 2000 Index

Russell 2000® Index is an unmanaged index that measures the performance of the smallest 2000 U.S. companies in the Russell 3000® Index.

### Russell 2000 Growth Index

Russell 2000® Growth Index measures the performance of those Russell 2000 Companies with higher price-to-book ratios and higher forecasted growth values.

*Investments cannot be made in an index.*

### Russell 2000 Value Index

Russell 2000® Value Index measures the performance of those Russell 2000 Companies with lower price-to-book ratios and lower forecasted growth values.

### MSCI ACWI ex USA Index

The MSCI ACWI Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets.

### MSCI EAFE Index (Developed Markets)

The MSCI EAFE Index Europe, Australasia, and Far East Index (EAFE) is a standard unmanaged foreign securities index representing major non-U.S. stock markets, as monitored by Morgan Stanley Capital International.

### MSCI European Monetary Union Index

The MSCI EMU (European Economic and Monetary Union) Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of countries within EMU.

### MSCI AC Asia Pacific Index

The MSCI AC Asia Pacific Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of Asia and Pacific region.

### MSCI Emerging Markets Index

The MSCI Emerging Markets Index is a market capitalization weighted index comprised of over 800 companies representative of the market structure of the emerging countries in Europe, Latin America, Africa, Middle East and Asia. Prior to January 1, 2002, the returns of the MSCI Emerging Markets Index were presented before application of withholding taxes.

### NASDAQ Composite Index

The NASDAQ Composite Index is a market-cap weighted index of the more than 3,000 common equities listed on the Nasdaq stock exchange.

### STOXX Europe 600 Index

The STOXX Europe Index represents 600 large, mid, and small capitalization companies across 18 countries of the European Region.

# Index Definitions

## Fixed Income Indices

### **Barclays U.S. Aggregate Index**

Barclays Capital U.S. Aggregate Bond Index is an unmanaged index that covers the U.S. investment-grade fixed-rate bond market, including government and credit securities, agency mortgage pass-through securities, asset-backed securities and commercial mortgage-based securities.

### **Barclays U.S. Interm. Gov/Crd Index**

Barclays Capital Intermediate U.S. Government/Credit Index (Barclays Capital Int Gov't/Credit) is an unmanaged index comprised of government and corporate bonds rated BBB or higher with maturities between 1-10 years.

### **Barclays U.S. Corporate Index**

The Barclays Capital U.S. Corporate Bond Index is designed to measure the performance of the U.S. corporate bond market.

### **Barclays U.S. Treasury Index**

The Barclays Capital U.S. Treasury Index is an unmanaged index that includes a broad range of U.S. Treasury obligations and is considered representative of U.S. Treasury bond performance overall.

### **Barclays Securitized Index**

The Barclays Capital U.S. Securitized Bond Index is an unmanaged index of asset-backed securities, collateralized mortgage-backed securities (ERISA-eligible), and fixed-rate mortgage-backed securities.

### **Barclays High Yield Index**

The Barclays Capital U.S. Corporate High-Yield Bond Index is an unmanaged index that covers the USD-denominated, non-investment-grade, fixed-rate, taxable corporate bond market.

### **BofA Merrill Lynch High Yield BB/B Constr. Index**

The BofA Merrill Lynch BB-B Global High Yield Index is a subset of The BofA Merrill Lynch Global High Yield Index including all securities rated BB1 through B3, inclusive.

### **Barclays 1-10 yr Municipals Index**

The Barclays Capital 1-10 Year Municipal Blend Index is a market value-weighted index which covers the short and intermediate components of the Barclays Capital Municipal Bond Index—an unmanaged, market value-weighted index which covers the U.S. investment-grade tax-exempt bond market.

### **Barclays Global Aggregate Bond Index**

The Barclays Capital Global Aggregate Bond Index is an index of global government, government-related agencies, corporate and securitized fixed-income investments.

### **Barclays Global Credit Index**

The Barclays Global Credit Index is the credit component of the Barclays Global Aggregate Index, an index of global government, government-related agencies, corporate and securitized fixed-income investments.

*Investments cannot be made in an index.*



# Index Definitions

## Alternative Investments Indices

### DJ UBS Commodity Index

The Dow Jones-UBS Commodity Total Return Index is composed of commodities traded on U.S. exchanges and it reflects the returns that are potentially available through an unleveraged investment in the futures contracts on physical commodities comprising the index plus the rate of interest that could be earned on cash collateral invested in specified Treasury Bills.

### DJ UBS Agriculture Subindex Index

The Dow Jones-UBS Agriculture Subindex is a sub-index of the Dow Jones UBS Commodity Index and is currently composed of seven futures contracts on agricultural commodities traded on U.S. exchanges.

### DJ UBS Livestock Subindex Index

The Dow Jones-UBS Livestock Subindex is a sub-index of the Dow Jones UBS Commodity Index and it is currently composed of two livestock commodities contracts (lean hogs and live cattle) traded on U.S. exchanges.

### DJ UBS Grains Subindex Index

The Dow Jones-UBS Grains Subindex is a sub-index of the Dow Jones UBS Commodity Index and it is currently composed of three futures contracts on grains traded on U.S. exchanges.

### DJ UBS Energy Subindex Index

The Dow Jones-UBS Energy Subindex is a sub-index of the Dow Jones UBS Commodity Index and it is currently composed of four energy-related commodities contracts (crude oil, heating oil, natural gas and unleaded gasoline) traded on U.S. exchanges.

### DJ UBS Precious Metals Subindex Index

The Dow Jones-UBS Precious Metals Subindex is a sub-index of the Dow Jones UBS Commodity Index and it is currently composed of two precious metals commodities contracts (gold and silver).

### DJ UBS Industrial Metals Subindex Index

The Dow Jones-UBS Industrial Metals Subindex is a sub-index of the Dow Jones UBS Commodity Index and it is currently composed of four futures contracts on industrial metals, three of which (aluminum, nickel and zinc) are traded on the London Metal Exchange and the other of which (copper) is traded on the COMEX division of the New York Mercantile Exchange.

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### MSCI ACWI Commodity Producers Index

The MSCI ACWI Commodity Producers Index is a component of the broader MSCI Commodity Producers Indices and covers large, mid and small cap companies across 45 Developed and Emerging Markets.

### Wilshire US REIT Index

The Wilshire US REIT Index measures U.S. publicly traded Real Estate Investment Trusts. It is a subset of the Wilshire US Real Estate Securities Index.

### S&P Global REIT Index

The S&P Global REIT Index measures the performance of real estate investment trusts in both developed and emerging markets.

### S&P Global Infrastructure Index

The S&P Global Infrastructure Index provides liquid and tradable exposure to 75 companies from around the world that represent the listed infrastructure universe including utilities, transportation and energy.

# Index Definitions

## Other Indices

### S&P/Case-Shiller 20-City Index

The S&P/Case-Shiller 20-City Index is a composite index of the home price index for 20 major metropolitan statistical areas in the U.S.

### VIX Index

The Chicago Board Options Exchange Market Volatility Index is a measure of implied volatility of S&P 500 index options, often referred to as the “fear” index.

### CPI Index

The Consumer Price Index is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care.

### Economic Cycle Research Institute (ECRI) Weekly Leading Index

ECRI Index is released each Friday by the Economic Cycle Research Institute, and identifies turning points in the economic cycle that are indicated by pronounced changes in the index. The index contains money supply data, stock prices, an industrial markets price index developed by the organization, mortgage applications, bond quality spread, bond yields, and initial jobless claims. An advantage of the index is that it is very timely. ECRI is a New York-based independent forecasting group.

### Conference Board Leading Economic Index® (LEI) for the U.S.

The leading economic index is composite average of several individual leading indicators. It is constructed to summarize and reveal common turning point patterns in economic data in a clearer and more convincing manner than any individual component – primarily because it smoothes out some of the volatility of individual components.

### Chicago Fed National Activity (CFNAI) Index

The Chicago Fed National Activity Index (CFNAI) is a monthly index designed to gauge overall economic activity and related inflationary pressure and it is a weighted average of 85 existing monthly indicators. A zero value indicates that the economy is expanding at its historical trend rate of growth; negative values indicate below-average growth; and positive values indicate above-average growth. When the 3-month moving average moves below -0.7 following a period of economic expansion, there is an increased likelihood that a recession has begun. When the 3-month moving average moves above +0.7 more than two years into an economic expansion, there is an increased likelihood that a period of sustained increasing inflation has begun (source: [www.chicagofed.org](http://www.chicagofed.org)).

### Citigroup Economic Surprise Index

The Citigroup Economic Surprise Index is a weighted historical standard deviations of data surprises (actual releases vs. Bloomberg survey median). A positive reading of the Economic Surprise Index suggests that economic releases have, on balance, been beating consensus. The indices are calculated daily in a rolling three-month window. The weights of economic indicators are derived from relative high-frequency spot FX impacts of 1 standard deviation data surprises. The index also employs a time decay function to replicate the limited memory of markets.

### European Countries Purchasing Manager Index

The PMI's are designed to provide a single figure snap-shot for the Eurozone.

It is based on a survey of over 3,000 business executives in the Euro area and it's designed to provide the most up-to-date picture of business conditions.

Anything above 50 indicates expansion; below 50, a contraction. The greater the divergence from 50, the greater the rate of change. The index is released by Markit Economics.

*Investments cannot be made in an index.*

# Disclosures

For further information, please visit our websites at

BMO Funds [www.bmofundsus.com](http://www.bmofundsus.com)

BMO Asset Management Corp. [www.bmogamus.com](http://www.bmogamus.com)

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