



The only certainty is uncertainty

Equities

Following two impressive years of Developed Market (DM) equity performance that was propelled by a cohort of US information technology heavyweights, early 2025 saw a reversal of market leadership.

In the US, the S&P 500 Total Return Index fell 4.2% in Canadian dollar terms, although this masked much greater weakness across the “Magnificent Seven¹”, leading US technology companies, which fell 15.0% in aggregate, reversing a modest portion of their gains generated in recent years (the rest of the S&P 500 Total Return Index cumulatively rose 0.6% in Q1). For Canadian investors, these returns were relatively unchanged by currency movements, with the Canadian dollar ending the quarter roughly unchanged.

The Canadian market fared better, as the S&P/TSX Composite Index rose 1.5%, which was propelled by a robust market for gold bullion that fostered a 20.0% gain for the Materials sector in Canada over the quarter. It was international DM, however, that stood out for performance, with the MSCI EAFE Total Return Index rising 6.9% in Canadian dollar terms over the quarter. An invigorated European response to looming Trump policies was the catalyst, prompting a major new infrastructure program in Germany and commitments to enhanced defense budgets in many European nations.

To give a sense of the broad strength, local equity indices rose 8.5% in the UK, 10.1% in France, 10.7% in Switzerland, 13.9% in Germany, 16.8% in Italy, and 22.1% in Spain in Canadian dollar terms for the quarter — across the entire MSCI EAFE Total Return Index, all 11 sectors rose, and gains were most pronounced for prime beneficiaries of these expansionary plans, such as banks and defense equipment manufacturers.

Policy action from the Trump administration was the central influence on equity markets over the quarter, and this seems likely to continue for the remainder of the year. The early read on his current Presidency suggests a continuation of a thrust and parry between the US and virtually all other nations on various policy matters, with public threats frequently altered or even retracted shortly thereafter, depending on the response. Daily stock volatility stands to rise in response, with investors best suited to sit tight amidst the swirling news flow. More positively, valuations for high-quality stocks in several sectors reside at very reasonable levels, allowing for a diversified portfolio to provide comfort and income in choppy waters.

Fixed Income

As with pretty much everything else in the quarter, fixed income assets experienced significant volatility in the first three months of the year as the heightened uncertainty related to US economic policy and its potential implications for global growth, inflation and policy rates roiled the marketplace.

Canadian bonds did, however, ultimately broadly finish the quarter in positive territory as sharp deterioration in sentiment among both Canadian households and businesses exacerbated risks posed by the looming threat of US tariffs to more than offset inflationary concerns, resulting in a further policy-cut-induced general decline in rates.

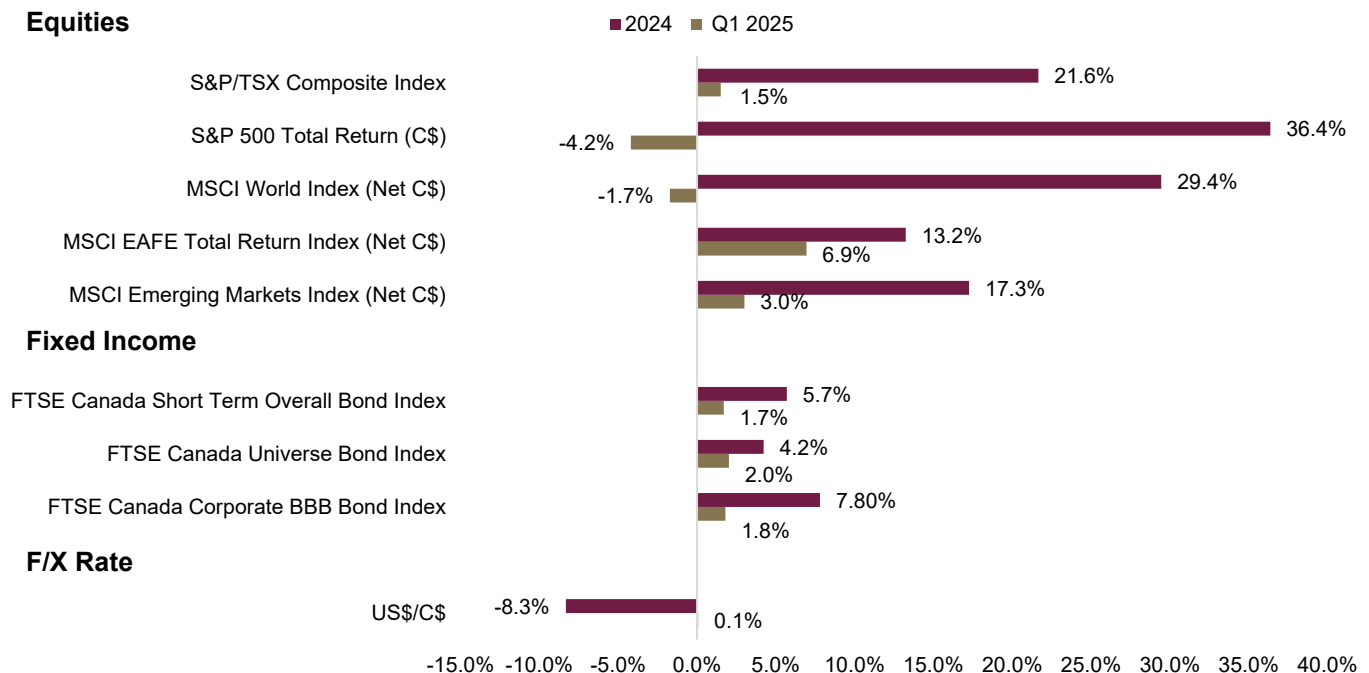


The broad benchmark FTSE Canada Universe Bond Index ended March with a decent +2.0% total return for Q1. The steepening of the yield curve in the period (two-year Government of Canada note yields fell 47 basis points in response to the Bank of Canada’s 50 basis points of rate cuts, while 10-year note yields declined just 26 basis points) meant short-term bonds (FTSE Canada Short Term Overall Bond Index +1.7%) kept pace with the more rate sensitive longer-duration securities (FTSE Canada Long Term Overall Bond Index +1.8%), while government bonds (FTSE Canada All Government Bond Index +2.1%) modestly outperformed corporate credit (FTSE Canada All Corporate Bond Index +1.8%) in the period.

Looking forward, it remains highly unlikely that uncertainty, and with it, volatility, will subside any time soon, which will keep investors in the market for safe income-generating assets but may continue to put upward pressure on credit spreads — with the latter more reflecting investor risk aversion than indications of deteriorating credit quality.

As well, the elevated risk of a domestic recession stemming from US policy will likely keep the market pricing in further monetary easing and exert downward pressure on rates, benefiting the asset class. That said, the Bank of Canada remains focused on managing inflation which could limit the magnitude of any policy response — the central bank explicitly noted in [March](#)² that monetary policy “cannot offset the impacts of a trade war” but that it “can and must ensure that higher prices do not lead to ongoing inflation” while also stating that they would not have cut rates [last month](#)³ had it not been for the threat of tariffs.

Market Indices Performance (C\$ - March 31, 2025)



Source Bloomberg: All figures stated in Canadian dollars as of March 31, 2025



Commentary

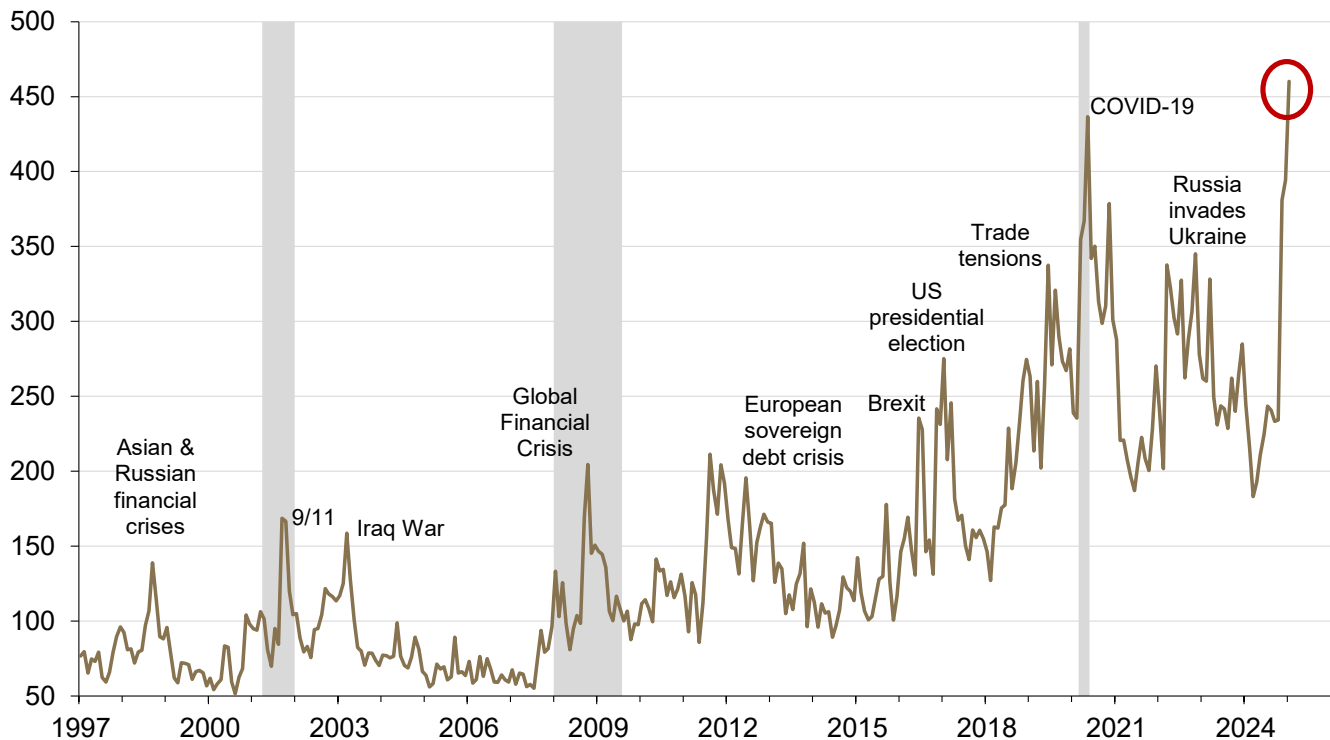
The first calendar quarter saw signs of continued and broadening economic and earnings growth, steady employment gains worldwide, and indications of still-moderating inflationary pressures. These factors contributed to more than half of the G20 central banks cutting rates in the period (while the rest, except for the Bank of Japan, remained on the sidelines). However, the positives of the ‘here and now’ clearly matter much less to consumers, businesses and markets than the unpredictability and related rising negative risks looming over what is to come.

Indeed, it is more than a little bit fascinating to see five years after the onset of a global health crisis — an event that disrupted every facet of everyday life and sent policymakers worldwide scrambling to do what they could to prevent economies from complete collapse — we’ve somehow managed to surpass those once unfathomable-records of uncertainty and pessimism.

As depicted below, the Global Economic Policy Uncertainty Index⁴ established a new high for the series’ three-decade history. Unsurprisingly, the key driver of this surge has been the developments out of the US since the transition in the White House took place at the end of January.

Global Economic Policy Uncertainty Index

(index; pre-2015 average=100)



Shaded regions represent periods of US recession; source: Guardian Capital using data from [PolicyUncertainty.com](https://www.policyuncertainty.com) to January 2025

IN REVIEW:

QUARTER 1



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The new Administration's aggressive turn against adversaries and (former) allies alike has roiled long-standing norms, with the persistent and escalating threat of tariffs representing another pandemic-like shock to global integrated supply chains that will bring cascading repercussions.

Further complicating matters is the fairly haphazard way in which the changes in trade policy are being rationalized and put into force. For example, the initial [Executive Order](#)⁵ levying tariffs on Canada cited the southward flow of fentanyl as the reasoning for the punitive measures despite [limited evidence](#)⁶ of the fact. On this latter point, the tariffs on Mexico and Canada have been delayed twice, while there is significant uncertainty about the breadth of levies that will actually be put in place on the April 2 "Liberation Day", not to mention how long such measures may be sustained.

The uncertainty about what policies may be in place even a week from now, let alone over the next month or four years, makes it incredibly difficult for consumers, businesses and investors to make spending and investment decisions. Such hesitation inevitably creates a headwind for economic activity and, in turn, places a considerable weight on sentiment — making it no surprise that survey-based indicators have registered notable declines so far this year, while risk assets have come under pressure (particularly those in the US).

However, it's worth remembering, there has yet to be a time where uncertainty alone has independently triggered a recession. The effects of uncertainty can make a bad situation worse, but in the absence of an actual material shock, such as highly restrictive trade policy not just being implemented but maintained — its impact could potentially tamp down on activity that is being supported by an otherwise constructive economic backdrop at the margin.

What this would imply is that while uncertainty and volatility are likely to remain the key watchwords for the foreseeable future, and risks to the downside remain elevated, there remains the scope for economic momentum to remain on a positive trajectory. It may well be the case that new opportunities arise in response to US policy developments, such as those stemming from the renewed era of government investment in Europe, while Canada and others could benefit from broadening their trade relationships — which could provide a fundamental support to markets that have undergone something of a valuation adjustment.



Endnotes

¹ Magnificent Seven = Alphabet (Google), Amazon, Apple, Meta (Facebook), Microsoft, Nvidia and Tesla.

²Bank of Canada, Press Releases, Bank of Canada reduces policy rate by 25 basis points to 2¾%, March 12, 2025, <https://www.bankofcanada.ca/2025/03/fad-press-release-2025-03-12/>

³Bank of Canada, Publications, Summary of Governing Council deliberations: Fixed announcement date of March 12, 2025, <https://www.bankofcanada.ca/2025/03/summary-governing-council-deliberations-fixed-announcement-date-march-12-2025/>

⁴The "Global Economic Policy Uncertainty Index" is a GDP-weighted average of national Economic Policy Uncertainty (EPU) indices for 16 countries that account for two-thirds of global output. Each national EPU index reflects the relative frequency of own-country newspaper articles that contain a trio of terms pertaining to the economy, uncertainty and policy-related matters.

⁵The White House, Presidential Actions, Imposing duties to address the flow of illicit drugs across our northern border, February 1, 2025, <https://www.whitehouse.gov/presidential-actions/2025/02/imposing-duties-to-address-the-flow-of-illicit-drugs-across-our-national-border/>

⁶U.S. Customs and Border Protection, Newsroom, Stats and Summaries, Drug Seizure Statistics, April 2, 2025, <https://www.cbp.gov/newsroom/stats/drug-seizure-statistics>

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