



Global Asset Allocation Perspectives & Investment Backdrop

MANAGED ASSET PROGRAMS
Second Quarter 2025 Preview

Market Review

A look back and ahead

The first quarter of 2025 was marked by economic and market turbulence driven by trade tensions and policy uncertainty. Overall, fixed income markets performed well, while equity markets were mixed and saw dramatic volatility. The U.S. experienced a sharp sell-off in its largest mega-cap and AI-focused companies – a strong reversal of 2024's performance for those stocks. Meanwhile, Canadian equities showed resilience, buoyed by strength in the materials sector, while international equities outperformed, supported by strong gains in China and Europe. The quarter underscored the complex interplay of geopolitical and economic factors shaping global markets and the importance of maintaining a well-diversified total portfolio approach. Here's a look back at what drove markets during the quarter and the key trends our team is closely monitoring.



FIXED INCOME

Canada Continues to Cut Rates, Bond Market Edges Higher:

- The Canadian bond market, represented by the FTSE Canada Universe Bond Index, ended the quarter up 2%.
- The Bank of Canada (BoC) cut its key interest rate twice during the first quarter, with a reduction of 0.25% each in January and March. With this backdrop, Canadian yields drifted lower over the quarter.
- The BoC Governing Council noted that the Canadian economy exceeded growth expectations in the previous quarter, bolstered by past policy rate cuts, but growth is expected to slow due to increasing trade conflict with the United States.
- Credit spreads widened as concerns over Trump tariffs took hold, with high yield spreads widening most over funding pressure and business uncertainty amidst tariffs.

Federal Reserve Pauses :

- In the first quarter, the Federal Reserve put a pause on their rate-cutting regime and kept rates unchanged at 4.25-4.5%, while signaling plans to reduce rates by 0.50% later this year.
- During their March meeting, Fed policymakers acknowledged inflation will rise this year primarily due to the impact of tariffs, though the magnitude and persistence of these effects remain greatly uncertain.

- The Fed raised inflation expectations over the short term with a strong employment backdrop and downgraded growth forecasts, reflecting their cautious stance amid evolving economic conditions.

Global Central Banks Navigate Rate Cuts Amid Uncertainty:

- The European Central Bank (ECB) cut rates by 0.25% in January and March; officials cautioned that U.S. tariffs and increased government spending, particularly on defense, could put pressure on prices and delay the disinflationary process, while emphasizing uncertainty around monetary policy and leaving the door open for future rate cuts.
- The United Kingdom also reduced interest rates once during the quarter, by 0.25% in February, while holding the rate stable at 4.5% in March, as policymakers adopted a wait-and-see approach amid stubbornly high inflation and global economic uncertainties.

Market Review (cont'd)



EQUITIES

U.S. Growth Stocks Tumble:

- The U.S. stock market started the year strongly, albeit with rich valuations and all-time highs, however as the new administration took office in January and announced their intentions to put tariffs on, the tone quickly changed.
- Increased trade aggressions and fears of stagflation – a mix of stagnant economic growth and rising inflation – triggered a significant market sell-off.
- U.S. stocks, represented by the S&P 500 Index, fell by 4.2% in Canadian dollars (C\$) for the quarter.
- The best-performing sectors of 2024 quickly became the worst performers of Q1 2025 as investors exchanged growth for value.
- The short-term outlook remains uncertain given the fluidity of President Trump's agenda. Meanwhile the labour market remains resilient, but consumer sentiment weakened amid growing inflation fears.

Canadian Materials Drive Market Gains:

- Canadian equities delivered modest returns this quarter, with the S&P/TSX Composite Index rising 1.5% (C\$).
- This performance was primarily driven by the Materials sector, which surged 19.9% (C\$), fueled by gains in precious metals prices, particularly gold, with geopolitical tensions increasing demand for safe-haven assets.
- Market volatility persisted throughout the quarter, as Canadian companies faced uncertainty stemming from escalating U.S. tariff threats and their potential implications for trade with Canada, its largest partner.

International Stocks Outperform:

- International stocks were also up, as represented by the MSCI EAFE Index, which returned 7.1% (C\$).
- Value outpaced growth and the strongest contribution came from China (+15.2%) and Europe (+10.7%).

To help guide the forward-looking positioning of Scotiabank's managed asset programs, the Multi-Asset Management team meets regularly with the Portfolio Managers at 1832 Asset Management L.P. This preview captures the team's current views and portfolio positioning.

Global Themes from the Multi-Asset Management Team



ECONOMIC GROWTH

Economic uncertainty is significantly elevated given the hawkishness of U.S. trade policy and tightening of financial conditions since the April 2nd announcement. Global growth was on stable footing based on incoming data; this may cushion some of the downside risks to the economy near term. A bigger risk is continued tightening of financial conditions as long as U.S. reciprocal tariffs and related confusion remain in place without resolution.



BUSINESS CYCLE

The business cycle is likely to move towards recessionary conditions as uncertainty weighs on consumption, investment, and the overall outlook from businesses.



MONETARY POLICY

Central banks are more likely to look through near-term price impact of tariffs and cut rates to support the economy, as financial market conditions have deteriorated materially.



INFLATION

Tariffs represent a supply shock, leading to higher prices in the near term and contributing to inflationary pressures. However, this inflationary impact may be counterbalanced by a reduction in demand, driven by tight financial conditions such as higher credit spreads and declining stock markets.



COMMODITIES

Commodity prices will remain under pressure due to heightened global economic uncertainty and ample supply, particularly in oil markets.



CURRENCIES

Safe-haven currencies like the Japanese Yen are benefiting from the increased level of uncertainty regarding the global economy.



RISK

Political risk has risen sharply, and financial conditions are expected to remain tight until there are clear signs of a resolution to U.S. trade hawkishness. While a policy reversal could present near-term upside risks, conditions may worsen further if the U.S. administration fails to ease its stance promptly.

Asset Allocation Positioning

	Outlook	Comments
FIXED INCOME		
Overall Fixed Income	0	Market fundamentals remain strong, however U.S. trade policy has weakened market sentiment causing uncertainty and volatility to soar. The market direction is highly path dependent on policy developments with upside and downside risks, hold neutral allocation for fixed income relative to equities. Overall levels of yields remain attractive from both income and potential capital appreciation perspectives.
Rates		
Canada and U.S.	0	Over the last year, the Bank of Canada continued to cut rates at a faster pace than the Fed, leading to the differential between U.S. and Canadian rates widening further. With markets pricing in an already widened differential, we have a long duration bias to U.S. bonds; however, hold a steepener to offset some of the risk if the U.S. long-end moves higher. The U.S. curve has steepened out considerably, but it is difficult to assess if the steepening was due to short-term technical factors or a long-term trend to increased term premium.
Global	+	Longer-term prospects for growth in Europe have improved following the German election, with the announcement of more fiscal spending to fund defense and infrastructure. In the near-term, growth remains challenged, and a slowdown in global trade would further affect the already weak growth profile. There is room for the European Central Bank to announce deeper cuts this year to help accommodate the negative growth impact. Higher inflation and budgetary concerns have driven yields materially higher in the United Kingdom, and we expect more easing over the year.
Credit		
Investment Grade	+	Credit spreads have widened off the lows seen over the year. Company fundamentals and balance sheets have improved over the recent years, which is attractive for companies with lower default risk that can ride through the current volatility.
High-Yield	-	High yield spreads have moved quicker than investment grade peers, due to a greater likelihood of default with forward-looking funding pressure and business uncertainty. Spreads increasing across the spectrum may create buying opportunities with a focus on credit research to identify stronger businesses.
EQUITIES		
Overall Equities	0	Headlines are currently moving equity markets rather than economic fundamentals. Although recession risks have risen significantly, many off-ramps exist that have the potential to lead to positive outcomes for risky assets. From a valuation perspective, recent declines have also increased the probability of rebounds. In the short term, a wait-and-see approach from a tactical perspective is prudent as the market fluctuates around Trump tariff headlines. Overall, given binary outcomes for equity markets are being significantly influenced by political factors, rather than economic data, a neutral stance is warranted at this time.
Region		
Canada	0	We have a neutral view of Canadian equities. Although the Bank of Canada has provided considerable easing to the Canadian economy, Trump tariffs are dampening the expectations for economic growth. Additionally, the outcome of the next Canadian election is also unclear, further increasing uncertainty. Similar to the investment rationale of our equities vs. fixed income, it is prudent at this time to maintain a neutral stance within our tactical relative equity decisions.
U.S.	0	We have a neutral view to U.S. equities. Although U.S. politics are driving all global equity markets, their effects on U.S. equities are perhaps the most acute. The potential for historically large tariffs has led to significant market volatility, with U.S. stocks experiencing sharp declines followed by sudden surges based upon policy shifts, such as the 90-day tariff pause announced in early April. This unpredictability complicates tactical decisions and increases the risk of significant losses from overweight or underweight positions, even with the possibility of sudden rallies.
International	0	We have moved to neutral international equities due to uncertainty related to the U.S. trade policy, which clouds the outlook for international markets. Earlier in the quarter there was a shift in allocations on the part of global investors back into European assets, attracted by low valuations and a paradigm shift in German fiscal policy to ease their debt brake to run deficits to fund defense and infrastructure investments. However, with large trade surpluses versus the U.S., European and Japanese equities, which dominate the international markets, are key targets of U.S. trade policy around tariffs. This uncertainty has kept us neutral.
Emerging Markets	0	We remain neutral on emerging market equities. While low valuations, technological advancements, and Chinese stimulus are positive for the asset class, the escalation in U.S. trade policy targeting China and other emerging markets with trade surpluses, such as Korea and Taiwan, raises concerns. Additionally, many less developed emerging markets are more economically sensitive. These offsetting factors of favourable conditions and trade uncertainty lead us to maintain a neutral stance.

Legend: ++ Overweight + Neutral-overweight 0 Neutral - Neutral-underweight - - Underweight

Performance – As at March 31, 2025

FIXED INCOME						
Bonds	3-Mth	6-Mth	YTD	1-Yr	3-Yr CAGR	5-Yr CAGR
FTSE Canada Universe Bond C\$	2.02%	1.98%	2.02%	7.65%	2.50%	0.88%
Universe Canada All Corporate C\$	1.81%	2.86%	1.81%	8.84%	4.38%	3.19%
Morningstar CAN High-Yield Fixed Inc C\$	0.79%	2.14%	0.79%	7.82%	4.66%	5.93%
ICE BofAML U.S. Corporate C\$	1.98%	-1.34%	1.98%	3.91%	0.45%	1.09%
ICE BofAML U.S. High Yield C\$	1.02%	7.71%	1.02%	14.48%	9.91%	7.46%
Bloomberg U.S. Aggregate Bond U\$	2.78%	-0.37%	2.78%	4.88%	0.52%	-0.40%
Bloomberg Global Aggregate U\$	2.64%	-2.60%	2.64%	3.06%	-1.63%	-1.37%
EQUITIES						
Canadian Equities	3-Mth	6-Mth	YTD	1-Yr	3-Yr CAGR	5-Yr CAGR
S&P/TSX Composite C\$	1.51%	5.33%	1.51%	15.81%	8.12%	16.98%
U.S. Equities	3-Mth	6-Mth	YTD	1-Yr	3-Yr CAGR	5-Yr CAGR
S&P 500 C\$	-4.20%	4.44%	-4.20%	15.13%	14.34%	18.86%
Dow Jones Industrial Avg C\$	-0.96%	6.49%	-0.96%	14.06%	14.00%	16.51%
NASDAQ C\$	-10.20%	1.67%	-10.20%	12.95%	13.22%	18.94%
Global Equities	3-Mth	6-Mth	YTD	1-Yr	3-Yr CAGR	5-Yr CAGR
MSCI World C\$	-1.61%	4.67%	-1.61%	14.34%	13.33%	16.93%
MSCI Asia Pacific ex-Japan C\$	2.17%	0.72%	2.17%	18.29%	5.99%	7.29%
MSCI Japan C\$	0.58%	3.25%	0.58%	4.50%	10.79%	9.44%
MSCI Europe C\$	10.72%	6.46%	10.72%	14.36%	13.23%	14.08%
MSCI Emerging Markets C\$	3.08%	1.14%	3.08%	15.55%	6.84%	8.62%

Source: Bloomberg, Morningstar

MULTI-ASSET MANAGEMENT TEAM

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Portfolio Manager

As Portfolio Managers for ScotiaFunds and Dynamic Funds managed-asset programs, the Multi-Asset Management Team oversees approximately \$121 billion* in multi-asset solutions and strategies. The Team is responsible for portfolio construction, asset allocation policy, and investment strategy research and selection. The Team is also involved in the due diligence and day-to-day management of all portfolio solutions.

Team supported by:

2 Associate Portfolio Managers | 8 Analysts

1 Trader & Portfolio Manager | 2 Portfolio Specialists

*As at December 31, 2024

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