FIRST QUARTER 2025 REVIEW & OUTLOOK
EXECUTIVE SUMMARY

16 April 2025

PORTFOLIO THEMES

- The global bull market will likely resume, despite recession fears and recent volatility.
- We expect previously out-of-favour categories, like European equities and Value, to lead global performance in 2025, building on their initial start in Q1, albeit with expectations for US to also fare well.
- Inflation risks remain contained, as global money supply growth is subdued and tariff influence appears far overstated, anchoring long-term interest rates within a stable range.

MARKET OUTLOOK

- **Tariff Fears Nearing Extremes:** With worst-case scenarios seemingly priced in, we believe there is likely upside relief if legislative or judicial resistance strengthens or if negotiations de-escalate trade tensions, but the chance that countries retaliate or rebuke the U.S. still exists, which would be a significant negative.
- **Corrections Are a Normal Part of Bull Markets:** Pullbacks are difficult to time but tend to be brief and constructive, often laying the groundwork for renewed upside.
- **Global Markets Should Surprise Higher:** Markets don't need extraordinary economic growth to perform well, and overly pessimistic sentiment, particularly outside the U.S., should set the stage for positive surprise.

For global equities, Q1 was a tale of two halves, capped by early April's sharp selloff over President Donald Trump's reciprocal tariff announcement. Equities notched new highs through mid-February, but volatility from there left global markets down -1.3% on the quarter.[i] Despite the up-and-down ride, Europe and Asia saw a much different first quarter than US markets. In keeping with our outlook, non-US developed market equities are vastly outperforming US.[ii] Value beat growth, and Tech lagged. Emerging markets also fared well, outperforming the developed world and ending the quarter up 2.93%, led by discretionary names.[iii]

As the full Review & Outlook will detail, tariffs are always negative economically, and the tariffs announced on "Liberation Day" were unprecedented in size and scope. The market's initial reaction to significant, fearful developments such as this is to quickly price in worst-case scenarios, often without giving much credence to more constructive outcomes. Although the worst scenario in this case could be quite bad for the US economy, possibly even recessionary, there are underappreciated alternatives with much more benign or even positive economic impacts that would lead to meaningful upside surprise. While fear over this is high today, it should fall moving forward as worried anticipation melts into acceptance and unknowns become known.

i Source: FactSet, as of 01/04/2025. MSCI ACWI Index return with net dividends, 31/12/2024 – 31/03/2025.

ii Source: FactSet, as of 01/04/2025. MSCI EAFE Index, S&P 500 index return with net dividends, 31/12/2024 – 31/03/2025.

iii Source: FactSet, as of 01/04/2025. MSCI Emerging Markets Index return with net dividends, 31/12/2024 – 31/03/2025.

That said, we are monitoring developments closely. Tariffs are a real negative, but their scope and how that relates to what markets have pre-priced matters most. So, to what extent are tariffs implemented, mitigated or avoided by companies? How will other countries react—with compromise or retaliation? And what of the many lawsuits and constitutional questions blanketed tariffs surely and immediately raise? The sheer scale and breadth of bureaucracy needed to inspect and collect all these tariffs simply doesn't exist today. Nor can non-US companies quickly or easily move production to the US given state regulations and permitting processes, to say nothing of construction and capacity.

When unknowns abound, we narrow them to a few most likely paths forward. Here are the three most plausible outcomes, in our view:

1. Strong pushback from the courts and Congress.

There is high likelihood courts will find some of these tariffs unconstitutional and need congressional legislation—at the very least, it seems likely to be hotly contested and could fall to the Supreme Court quickly. Republicans have slim majorities in Congress as it is—only a few defectors, perhaps from battleground states and districts, could sink all this very quickly. Already, a symbolic Senate vote disavowing Trump's Canada tariffs passed 2 April with Republican defectors. It may never become law, but it hints at the underlying reality. Markets likely see relief from any mitigation here.

2. Countries come to the table to negotiate.

So far, most countries have demonstrated a willingness to negotiate. Many see Trump's tactics as starting points for negotiation, the goal being to have other tariffs reduced toward US exports. Trump himself offered this path. Perhaps. If true, market relief would likely be swift as a much better-than-feared outcome arises through compromise. Markets demonstrated some evidence of this on 9 April when President Trump announced 90-day delays on the recently issued "reciprocal" tariffs to all countries, with the exception of China, lowering rates to the universal 10%.

These first two possibilities, or some combination of them, are the most likely in our view. Either would fit the correction form—again, the disproportionate fear of a plausible negative ultimately fueling the bull market. However, a third, and more negative possibility is also on the table:

3. Countries react with hostility to tariffs, retaliate, and possibly collude to rebuke the US.

Such a scenario could be a significant negative. Up to this point we have argued implemented tariffs don't have the scale to erase global GDP growth. But a full implementation—with retaliation—of tariffs would constitute a meaningful negative. This is an unlikely outcome, in our view, but not impossible.

Regardless of scenario, consider the plan's viability. Again, the bureaucracy, staffing and systems necessary to inspect imports and collect all these new tariffs simply doesn't exist today. This also argues for actual collection versus reality to be far less than most fear.

Our base case remains: We still think US equities should do fine this year. But we believe equities outside America likely lead, as they did in Q1. Tariff turmoil shows this, in our view. While April's volatility struck markets globally with few exceptions, Q1 ended with much of Europe up low double-digits this year, as well as much of Asia. We suspect this leadership will persist beyond the correction—if not during it.

Last quarter's Review noted a correction was possible at any time, for any or no reason. Of course, we didn't forecast one starting right after that went to press—we never try forecasting or timing corrections and similarly short-term moves. The reason for this is simple: Not all market negativity is the same. They usually feature a big scary story or two—fanning huge fears—that draw vast attention from pundits and individual investors. They are frightening and psychologically painful, but normal in bull markets—healthy, even. We know they can be trying and difficult to endure in the moment. But they reset sentiment lower and rebuild the wall of worry, setting the stage for the bull market's next move higher.

Bear markets are deep, grueling, usually slower and longer-lasting declines exceeding -20%, typically fueled by negative fundamentals like recession. They start slowly and grind lower until panicky throes strike late. The combination of a slow rolling top, longer duration and fundamental deterioration give evasive action during a bear market a much higher probability of success if the conditions warrant.

Corrections are different, both starting *and ending* without warning. The danger corrections present isn't the decline itself, but the fight-or-flight response it triggers from investors. Surrendering to this with drastic portfolio changes to limit downside usually backfires terribly, which is why we are thoughtful before making any substantial repositioning to the portfolio.

Whenever volatility strikes, we work carefully and diligently to determine whether it is a bear market or correction. Q1's downturn has all the classic correction hallmarks. As noted, world and US equities stood at record highs in mid-February. The S&P 500's decline breached -10% in 16 trading days.[iv] Sentiment darkened rapidly, with tariffs and American geopolitical gyrations emerging as the scary stories, reaching fever pitch after 2 April's "Liberation Day" announcement.

Corrections are impossible to time at their start or end. Because they hammer sentiment, they typically end sooner than everyone anticipates, with a V-shaped bounce and march to new highs and beyond. We expect that as 2025 unfolds. Resurgent recession talk still looks unfounded, we believe. The global economy has pockets of weakness as well as strength, but the balance is more positive than most perceive. Markets also don't need perfection to move higher. They are efficient discounters of all common fears, forecasts and opinions.

What moves equities is how reality unfolds relative to current expectations over the next 3 – 30 months. The balance should now be positive surprise, in our opinion. With sentiment so dour, things even going bad—but less bad than feared—would bring big bullish relief. This is what we expect for the balance of 2025.

iv Source: FactSet, as of 31/03/2025.

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INDEX DESCRIPTIONS

MSCI ALL COUNTRY WORLD

MSCI All Country World Index is a free float-adjusted market cap-weighted index that is designed to measure the equity market performance of developed and emerging markets. The MSCI ACWI Index consists of 23 developed country and 24 emerging market country indexes. Unless otherwise specified, returns shown include dividends after deducting estimated withholding taxes. MSCI calculates estimated withholding taxes using the maximum rate of the constituent company's country of incorporation applicable to non-resident institutional investors that do not benefit from double-taxation treaties.

MSCI EMERGING MARKETS

MSCI Emerging Markets Index is a free float-adjusted market cap-weighted index that is designed to measure equity market performance of emerging markets. The MSCI Emerging Markets Index consists of 24 emerging market country indices. Unless otherwise specified, returns shown include dividends after deducting estimated withholding taxes. MSCI calculates estimated withholding taxes using the maximum rate of the constituent company's country of incorporation applicable to non-resident institutional investors that do not benefit from double-taxation treaties.

S&P 500

The S&P 500 Index is a capitalization-weighted, unmanaged index measuring 500 widely held US common equities of leading companies in leading industries, representative of the broad US equity market.

MSCI EAFE

The MSCI EAFE Index is designed to represent the performance of large and mid-cap securities across 21 developed markets, including countries in Europe, Australasia and the Far East, excluding the U.S. and Canada. The Index is available for a number of regions, market segments/sizes and covers approximately 85% of the free float-adjusted market capitalization in each of the 21 countries.