Equitable Asset Management Group

Market Comments

July 2025

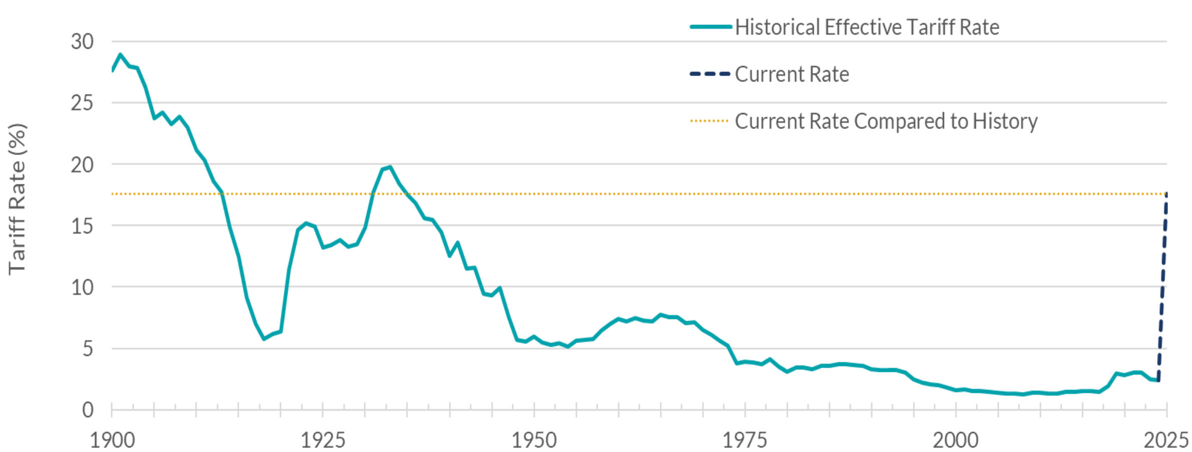
Key Takeaways for Q2:

- **Markets were very volatile in April to start Q2 but calmed as the quarter progressed.** Volatility was driven mostly by headlines about tariffs, but other fiscal policy developments also had an impact.
- Equity markets sold off sharply at the start of the quarter, continuing Q1's weakness. Markets rebounded sharply once worst-case fears over tariffs eased. The markets continued to rally through the quarter as trade negotiations progressed. Stronger-than-expected corporate earnings also boosted markets. **Despite the shaky start to the quarter, most global equity markets set new all-time highs in Q2**.
- **Canadian bond markets delivered slightly negative returns in Q2**. Weak performance was driven by rising interest rates, which outweighed the impact of tighter credit spreads. Higher interest rates hurt the performance of longer-term bonds most.
- **Both the Bank of Canada and the U.S. Federal Reserve adopted a wait-and-see approach.** They each held rates steady during Q2, awaiting greater clarity on the impacts of tariffs on both growth and inflation before considering further cuts.

Economic and Market Update

Economic Summary: Most indicators of economic activity in the U.S. continued to expand at a decent pace. However, GDP data for the first quarter came in weaker than expected, as higher imports ahead of anticipated tariffs and weaker spending by consumers weighed on Q1 GDP. That said, GDP growth is expected to bounce back in Q2. Tariffs will likely continue to be an evolving story, with potential impacts on both economic growth and inflation. Those impacts will remain uncertain until trade agreements have been finalized.

Fig. 1: U.S. Average Effective Tariff Rate



source: "State of U.S. Tariffs" by the Budget Lab at Yale at budgetlab.yale.edu

In early April, President Trump announced larger-than-expected reciprocal tariffs, with the impact most notable on trade with China. However, progress followed with a 90-day pause in tariff implementation. The U.S. then reached trade agreements with the UK, China, and Vietnam. Negotiations with other major trade partners are ongoing. The conflict between Israel and Iran raised inflation concerns, due mostly to the possibility of higher oil prices. Those concerns eased following a ceasefire. Congress passed Trump's tax cut and spending bill, raising concerns about its potential impact on the U.S. fiscal burden. Meanwhile, U.S. labour market conditions remain resilient, with the unemployment rate remaining low. Inflation has eased slightly but remains above the Federal Reserve's target. Amid heightened uncertainty, the Federal Reserve held interest rates steady at 4.25%–4.50% at both of its meetings in Q2. Chair Jerome Powell stated that the Fed is "well positioned to wait for greater clarity before considering any adjustments to our policy stance."

In Canada, tariffs and trade-related uncertainty continue to weigh on the economy. A pull-forward of exports and inventory accumulation ahead of tariffs helped keep first-quarter GDP firm, but growth is expected to slow in the second quarter. The labour market has weakened, particularly in trade-sensitive sectors. Inflation remains within the Bank of Canada's 1–3% preferred range. However, core CPI remains above the Bank's preferred 2% target. Canada's fiscal deficit is expected to widen as Prime Minister Mark Carney aims to fast-track infrastructure development and increase defense spending. Amid ongoing trade uncertainty, the Bank of Canada held its policy rate at 2.75% during its April and June meetings. Governor Tiff Macklem signaled the Bank's readiness to cut rates further if economic conditions deteriorate.

Bond Markets: During Q2, the FTSE Canada Universe Bond Index returned -0.6%. Yields for Canadian bonds rose across all maturities over the quarter. That reflected reduced expectations for rate cuts by the Bank of Canada and a higher risk premium on long-term debt. The impact of higher yields on government bonds was offset in part by tightening of credit spreads on provincial and corporate bonds.

	2nd Quarter	2025 Performance
US 10 Year	2 bps	-34 bps
Canada 10 Year	31 bps	5 bps
Canada Aggregate Bond	-0.5%	1.2%
US Aggregate Bond*	1.3%	4.0%

*Returns are calculated based on representative ETFs

Overall corporate bonds saw a positive return for the quarter and outperformed government bonds, in part due to the strong recovery in credit spreads that started in late April. While corporate issuance slowed considerably in April due to increased trade policy uncertainty, issuance in the Canadian bond markets during May and June were robust. There were 83 deals during Q2 that combined to raise $37 billion for issuers. June 2025 was the 3rd busiest month for issuance on record. We continue to expect higher credit spreads as the U.S. tariffs impact global growth.

As such, we have maintained our conservative view with a bias towards shorter corporate bonds but remain ready to invest in longer corporate bonds as valuations become attractive.

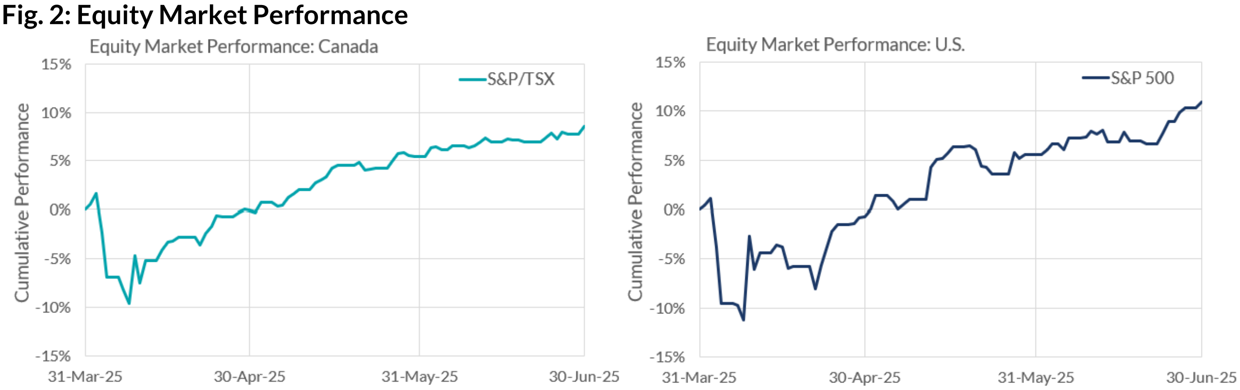
Stock Markets – Overview:

	2nd Quarter	2025 Performance
S&P 500	10.9%	6.2%
S&P/TSX Composite	8.5%	10.2%
EAFE	5.1%	8.3%

Returns are in local currency terms

Having done a round-trip following April tariff announcements, technology, consumer discretionary and industrial companies propelled the U.S. equity market to another record high. The S&P 500 ended the quarter up about 11%, outperforming Canadian and international markets. Canadian equities gained 8.5% in Q2, buoyed by front-loaded demand that benefited the Materials sector, while Financials recovered from a poor Q1. Meanwhile, as risk sentiment stabilized following the 90-day tariff pause and U.S. equities regained momentum, the appeal of the "Sell America" trade diminished. As a result, Europe, Australasia, and the Far East (EAFE) markets finished the quarter with a more modest gain of just over 5%, lagging the sharper recovery seen in North America.

Fig. 2: Equity Market Performance



source: Bloomberg

U.S. Equities: The U.S. equity market staged a V-shaped recovery on strong company earnings data in the second quarter. A stable job market and muted inflation reinforced the view of a resilient U.S. economy. At a company level, we observed positive corporate earnings surprises, steady profit margins and better-than-expected forward earnings guidance. Together they underpinned the equity market's sharp reversal to the upside. Market breadth also improved over the quarter, with strength extending beyond Technology to include Industrials and Financials. That signalled that the market rally was supported by investors' confidence in the U.S. economy.

Furthermore, structural investment trends in artificial intelligence (AI) continued to accelerate, highlighted by rising enterprise capex in data centres. Beyond AI, Circle, a blockchain-based platform that supports stablecoin issuance, tokenized assets, and digital payment infrastructure, conducted a successful IPO. Its share price jumped 485% from its listing price as of quarter-end. On June 17, the U.S. Senate passed the Guiding and Establishing National Innovation for U.S. Stablecoins (GENIUS) Act, a regulatory framework for use of tokenized assets. While investors wait for the House's decision, equity price actions suggest that the policy environment is increasingly supportive of blockchain innovation and digital efficiency.

Canadian Equities: Canadian equities posted solid gains in Q2, with Financials overtaking Materials to lead the market higher. Momentum from the Materials sector, which benefited from the pull-forward demand related to U.S. tariff uncertainty, faded toward quarter-end. Meanwhile, cooling inflation and muted domestic growth pushed investors towards high-quality, high-dividend-paying companies. Notably, banks significantly outperformed the broader market, as investors favoured their stable corporate fundamentals. Energy surged briefly amid escalating geopolitical tensions, but those gains proved short-lived.

In recap, investors in the Canadian market faced slowing resource demand and a stalling domestic economy, which fueled increased interest in high-quality, high-dividend-paying companies. That is a trend we expect to continue going forward.

Bottom line:

Markets remain heavily influenced by sentiment, with U.S. policy developments and ongoing tariff negotiations continuing to cause periodic volatility. However, there is little evidence of deterioration in the hard data to date. As such, we continue to anchor our positioning on underlying data rather than market narratives. Looking ahead, the combination of a structurally higher-for-longer interest rate environment and increasingly pro-growth policy backdrop presents selective opportunities. In the U.S., this favours high-quality growth stocks, particularly within Technology, where strong balance sheets and long-term thematic tailwinds remain intact. In Canada, Financials, especially the relatively inexpensive banks, present a more compelling opportunity as earlier tailwinds from pull-forward demand are beginning to wane. While we remain constructive, we are mindful of elevated equity valuations and continue to closely monitor macro conditions and policy developments for signs of inflection.

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