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Private Wealth

GLOBAL EQUITY AND INTERNATIONAL STRATEGIES

First Quarter 2025 Review

Q1 2025 Review

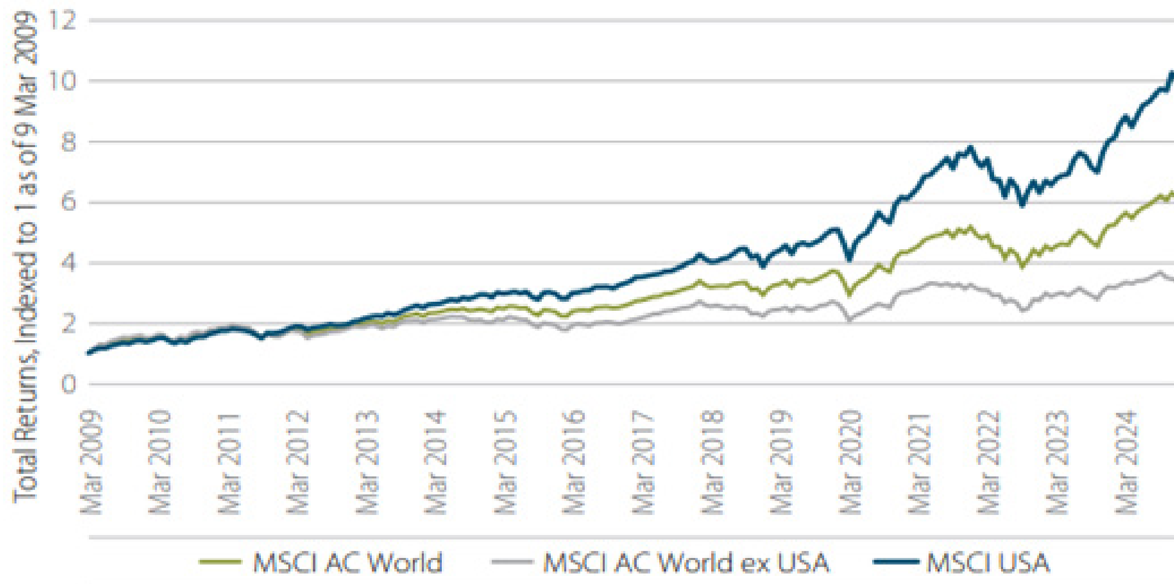
In a reversal of fortunes from previous quarters, the S&P 500 was a laggard among the large developed markets during the first quarter of 2025. Given that the S&P 500 had generated 2 consecutive years of 20%+ returns in 2023 and 2024, it is not surprising that some of the gains from the last 2 years have been given back. The Magnificent Seven (Amazon, Apple, Alphabet, Meta, Microsoft, NVIDIA, and Tesla) were key detractors of performance for the S&P 500 with these 7 stocks down more than 15% on average during the first quarter. One of the key factors that drove the weakness in the S&P 500 was renewed fears about the possibility of a recession in the US. This fear was largely driven by the uncertainty surrounding the tariff policy that is being implemented by the Trump administration. Outside of the U.S., returns were mixed with positive gains in Europe and Canada, and a negative return in Japan.

Q1 2025 Global Stock Market Returns

Index	Geographic Region	Currency	Price change	Total return with dividends
MSCI World	Global	US$	-2.1%	-1.7%
S&P 500	United States	US$	-4.6%	-4.3%
Euro Stoxx 600	Europe	Euro	+5.2%	+5.9%
Tokyo Stock Exchange	Japan	Yen	-4.5%	-3.5%
TSX	Canada	CAD$	+0.8%	+1.5%

Source: Bloomberg

The reversal of fortunes that occurred in the first quarter has been a long time coming given that U.S. markets have significantly outperformed global markets for a long time as illustrated in the chart below.



This period of U.S. market outperformance goes all the way back to 2009 when the stock market bottomed during the Great Financial Crisis. From March 31, 2009, to December 31, 2024, the MSCI USA Index generated a cumulative total return of 903%. This compares with a cumulative total return of 263% for the MSCI World excluding USA index. The extended duration of U.S. market outperformance in this cycle is rare as shown in the chart below. It has also given rise to the expression 'U.S. Exceptionalism', a concept associated with U.S. stocks outperforming the rest of the world.

US and International Markets Have Moved in Cycles

While we hope US stocks continue to perform well, history suggests that international stocks may soon have their day in the sun. Since 1975, the outperformance cycle for US vs. international stocks has lasted an average of more than eight years. We're currently 13.8 years into the current cycle of US outperformance based on 5-year monthly rolling returns.

US Equity vs. International Equity 5-Year Monthly Rolling Returns (1975-2024)

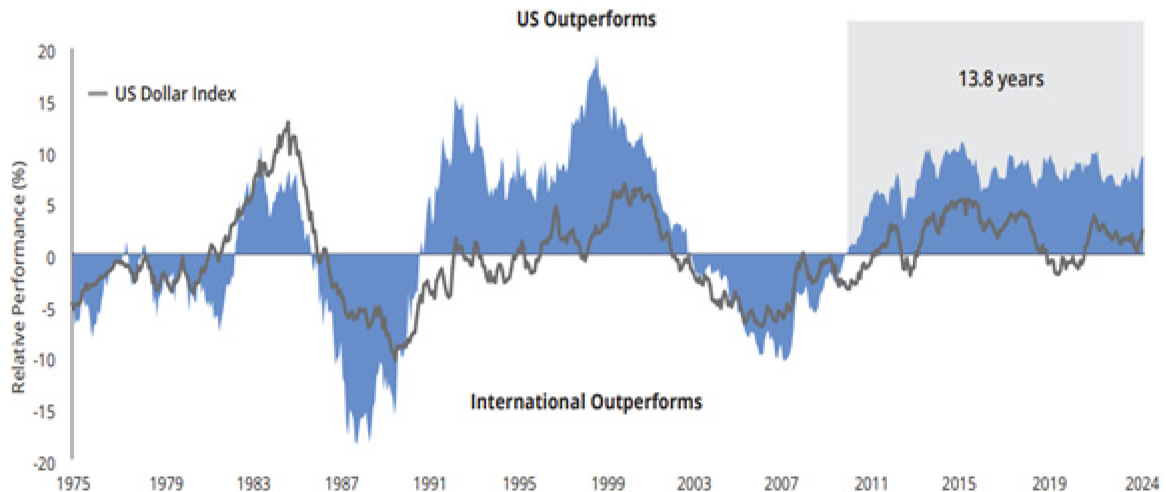


Chart Data: 1/31/75-12/31/24. The chart shows the values of the S&P 500 Index's returns minus the MSCI World ex USA Index's returns. When the line is above 0, domestic stocks outperformed international stocks. When the line is below 0, international stocks outperformed domestic stocks.

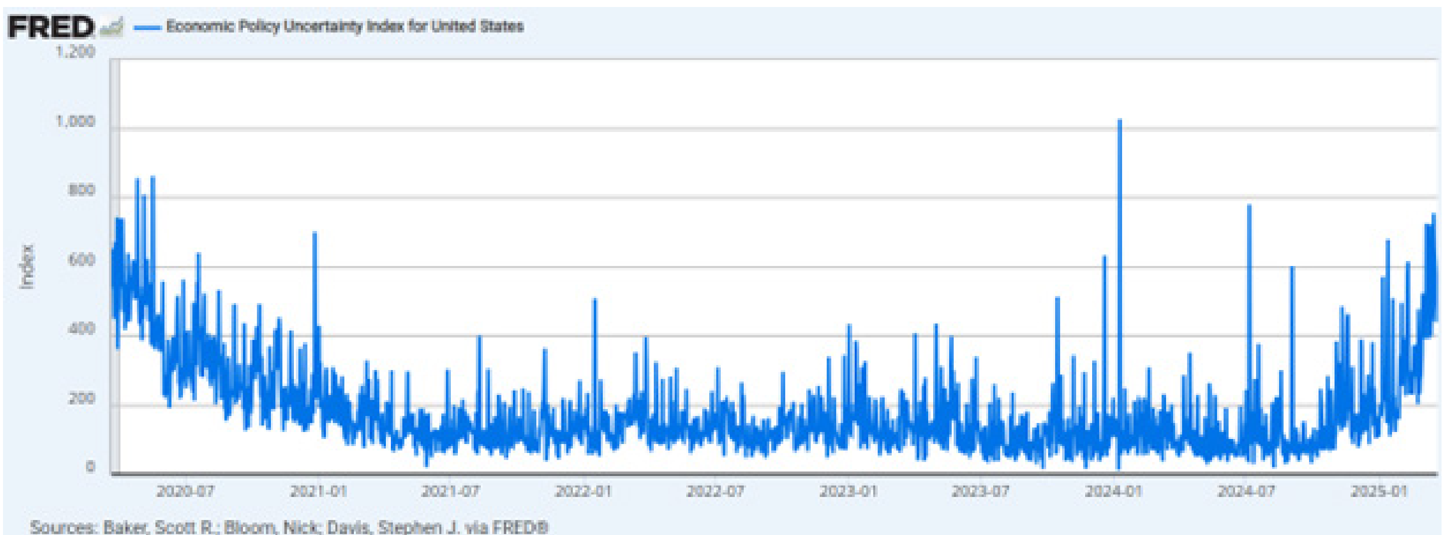
Data Sources: Morningstar, Bloomberg, and Hartford Funds, 1/25.

As shown in the chart above, U.S. and International markets have historically taken turns outperforming each other with the average outperformance cycle for US versus International stocks lasting approximately 8 years. Given that the current cycle of US outperformance is well above the historical average, a reversion to the mean was likely to occur at some point. We believe that 2 key catalysts have emerged that help to explain the reversal of fortunes that occurred during the first quarter. These catalysts include the policy proposals of Donald Trump and sweeping legislative changes that were recently announced in Germany.

During his first few months as U.S. President, Mr. Trump proposed a series of significant policy changes including tariffs, immigrant deportation, and initiatives to reduce the Federal deficit. With regards to tariffs, the goal is to bring manufacturing back to America. Since 2001, America's share of global manufacturing has declined by a significant amount with some estimates pointing to a 15% share, which is down from 25% in 2001. One of the concerns related to bringing back manufacturing to the United States is that it will be very expensive. It has been estimated that U.S. manufacturing workers make approximately US$25-30 dollars per hour, which compares with about US$3-5 per hour for Mexican manufacturing workers. In addition, there is also the cost associated with opening new manufacturing plants at a point in time where inflation has increased. In terms of immigrant deportation, one of the key concerns is that there is already a shortage of manufacturing workers in the United States. According to McKinsey & Company, there is currently a shortage of approximately 1.9 million manufacturing workers in the United States. If mass deportation is carried out, the U.S. would have to potentially

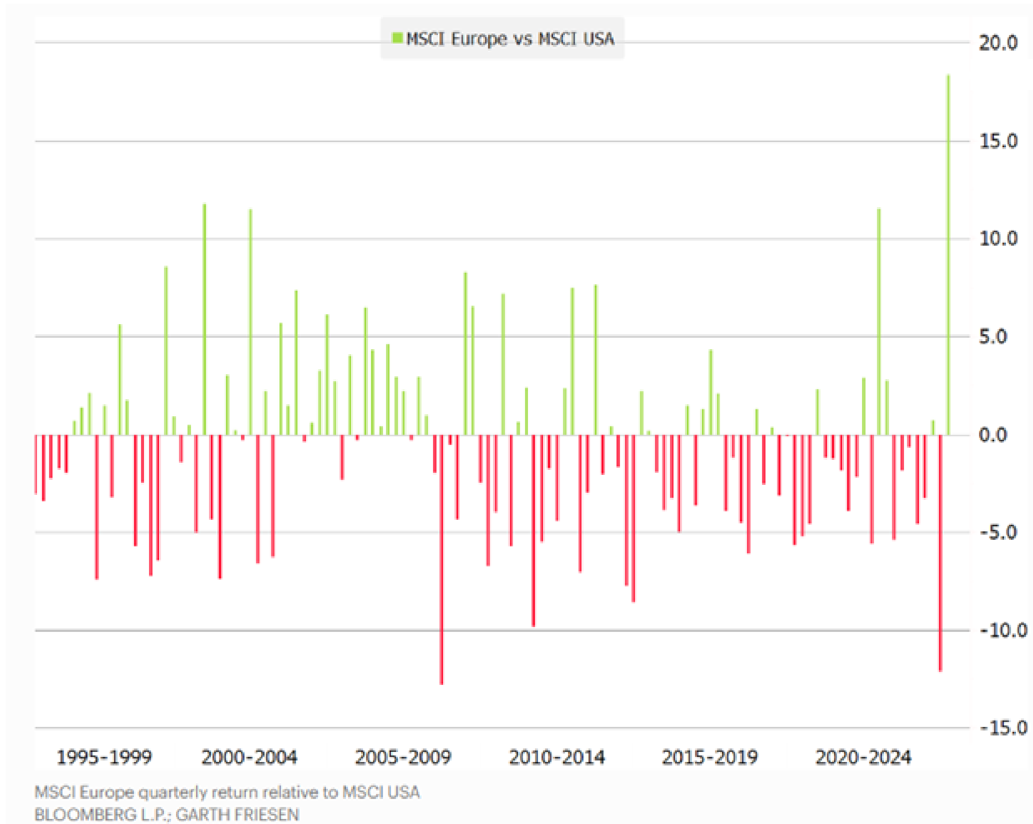
contend with the loss of hundreds of thousands of unauthorized workers who are essential to critical industries such as agriculture, construction, and hospitality. Finally, there is the issue of reducing the Federal deficit. A key aspect of this initiative includes a significant reduction in government workers, an effort that is being led by a new department called the Department of Government Efficiency (also known as DOGE). While the goal of reducing the U.S. Federal deficit is widely viewed as a very positive development, terminating government workers could push up the unemployment rate in the U.S. if these workers cannot find new jobs.

Although the hard economic data has not deteriorated significantly, there are rising concerns about the cumulative impact that tariffs, immigrant deportation, and DOGE layoffs will have on the U.S. economy. Economists have started to lower their expectations for economic growth while increasing their expectations for inflation. In the near-term, the uncertainty around tariffs has the potential to impact household and corporate spending decisions. The rising level of uncertainty is being reflected in the U.S. Economic Policy Uncertainty Index as illustrated in the chart below.



Given that the stock market does not respond well to higher levels of uncertainty, it's not surprising that the U.S. markets were weak during the first quarter of the year.

Switching gears to international markets, it makes sense to begin with Europe given that European equities just delivered one of the strongest quarterly performances in decades. Euro stocks also outperformed the S&P 500 by more than 15.0% in U.S. dollar terms, the widest margin in over 30 years as seen in the chart below.



MSCI Europe quarterly return relative to MSCI USA
BLOOMBERG L.P.; GARTH FRIESEN

It was only 6 months ago that former European Central Bank president Mario Draghi delivered a very downbeat message regarding European's competitiveness. So why did European stocks perform so well? While there are several factors that can help to explain it, the sweeping announcements that were recently made in Germany were certainly helpful. On March 18, 2025, Germany's Federal Parliament voted in favour of a landmark bill that plans to unlock hundreds of billions of euros for defence and infrastructure projects. The passing of this bill marks one of the largest fiscal policy shifts in postwar Germany. The bill will also loosen the country's constitutionally mandated debt limits. Under the new framework, defense and security expenditures above a certain threshold will be exempt from Germany's debt brake. The debt brake is a fiscal constraint that was introduced in the aftermath of the 2008 global financial crisis to promote financial stability. These new fiscal measures could provide a significant boost to Germany's economy and should also have a positive flow through impact to other economies throughout the Eurozone. With a debt-to-GDP ratio of just 62%, Germany has considerable room to manoeuvre with fiscal policy. From our perspective, Germany's new-found commitment to fiscal stimulus could mark the beginning of a renewed cycle of capital and infrastructure investment.

The key question about Europe is whether the rally during the first quarter can continue. We do believe there are several tailwinds that can support European equities going forward. These tailwinds include both fiscal policy on the back of Germany's recent announcements and monetary policy with multiple interest rate cuts expected for 2025. Earnings revisions for Europe have been positive and relative valuations versus the U.S. remain favourable. There is also the possibility of a ceasefire in the ongoing war between Ukraine and Russia. Although Europe's rally appears to be well supported, the region must deliver on promised fiscal stimulus, manage growing geopolitical risks, and navigate the uncertainty surrounding tariffs before investors can be confident in the durability of the rally. Stay tuned.

Outside of Europe, we are potentially seeing some green shoots in China. For the month of March, China's manufacturing activity expanded at the fastest pace in a year with new orders boosting production. This reading could provide officials some reassurance that recent stimulus measures are starting to support China's economy. Meanwhile, Japan's economy continues to expand at a modest pace although the October to December quarter grew at a slower pace than initially reported. At the same time, government officials have expressed concerns about the risks stemming from Donald Trump's tariff policies given the export-oriented nature of Japan's economy. Overall, we are encouraged by what we see in the international markets outside of the United States, notwithstanding the risks associated with forthcoming tariffs.

Outlook for 2025

Bringing it all together, we believe the risks to the global economy have increased given the uncertainty surrounding U.S. tariff policy. What happens next will depend on how the various countries respond to the U.S. tariffs. If the recently announced tariffs lead to productive negotiations, then it could result in favourable outcome for the global economy. If China, Europe, and other countries decide to retaliate instead of negotiate, then the risk of a global recession will increase. Given the increased uncertainty, we have raised cash in our portfolios. While there remains uncertainty in the near term, we are more constructive on a longer term perspective given our expectation of rate cuts in the U.S. and Europe, accelerating economic growth in Europe in the years ahead on the back of Germany's announcement, as well as ongoing stimulus measures in China.

Portfolio Review:

During the first quarter, we established several new positions in our Global and International portfolios. In our Global strategy, we established new positions in 3i Group, Autodesk, Cadence Design, Progressive Corp, and Stantec. In the International strategy, we initiated new positions in Adyen, Aon, Hannover Rueck, Publicis, Reply, and Sony Corp. A brief description of each new holding can be found in the Appendix.

Phil D'Iorio
Lead Manager,
Cumberland* Global and International Equities
April 3, 2025

Appendix A – Company descriptions for new positions added to the Global Strategy

3i Group is a private equity company with over 70% of its net asset value accounted for by a company called Action. Action is a leading European-based store concept that has consistently outperformed the industry over the last decade. Starting with 1 store in Netherlands 30 years ago, Action has grown to become Europe's fastest-growing non-food discounter. With over 2,900 stores across 12 countries, Action offers a constantly changing selection of 6,000 products at unbeatable prices. Action has a strong track record of double-digit sales growth driven by a treasure hunt shopping concept and merchandising around 14 core necessities that keeps traffic high. The company's private label product offering enhances growth and is also accretive to margins. Management believes it can expand its current store base of approximately 2,900 stores to potentially a further 4,700 stores across its existing footprint. Management is also considering the possibility of expanding its store base outside of Continental Europe. We believe there is a long runway of growth ahead for Action.

Autodesk is a U.S. based software company that is the leading player in design, engineering, and entertainment software. The company provides customers with end-to-end solutions in computer-aided design (CAD), computer-aided manufacturing (CAM), computer-aided engineering (CAE), building information modeling (BIM), product lifecycle management (PLM). The company's broad-based set of tools that cater to numerous industries and its strong organic growth is complemented through tuck-in acquisitions. Their cloud offering is shifting to a platform service to provide better workflow for its customer base resulting in improved retention. Management has maintained a mid-term margin target 250 basis points above its FY 2024 level which should help drive sustained earnings growth for many years.

Cadence Design Systems (CDNS) is a leading provider of Electronic Design Automation (EDA) software, a critical tool used to design a range of chips, from analog sensors to high-end logic chips used in artificial intelligence. Its dominant market position, a duopoly alongside Synopsys, offers stability and pricing power. The growing trend of custom chip design, particularly in AI and ARM-based chips, is increasing demand for its software. Cadence has a history of generating attractive returns on invested capital as well as strong organic revenue growth, driven by its essential role in the chip design process.

Progressive Corporation is a leading insurance holding company in the United States providing insurance coverage for personal auto, commercial auto, and property lines. As the second-largest private passenger auto insurer and the top commercial auto insurance writer, Progressive's scale leads them to superior profitability. Progressive's competitive advantage stems from its lowest expense ratio in the industry which allows it to underwrite the most competitive auto policies. Its leading telematics programs gives the company an advantage in customer acquisition as well as underwriting performance with improving loss ratios. Given its position as the low-cost provider, Progressive is winning market share while also generating industry leading growth. We believe that Progressive should continue to gain share and could possibly double its revenues within 5-7 years.

Stantec is a global leader in sustainable engineering, architecture, and environmental consulting. The company leverages its expertise & technology to deliver solutions to its customers to help them manage aging infrastructure, demographic and population changes, the energy transition, and more. Although the company is involved in several end-markets, it has become increasingly focused on water. In recent years Stantec has delivered strong organic growth which has been complemented by a series of acquisitions. With more than 50% of sales derived from the U.S., Stantec is well positioned to benefit from major US legislation like the Inflation Reduction Act, the Chips Act, as well as the re-shoring trend as more manufacturing is brought back to the United States.

Appendix B – Company descriptions for new positions added to the International Strategy

Adyen is a financial technology platform which offers end-to-end payment services to big enterprises as well as small and medium sized businesses. Adyen offers a full-service financial technology platform, managing the entire payments lifecycle through a single integration—covering gateway, risk management, processing, issuing, acquiring, and settlement services. With direct connections to both local and international card and banking networks, the company emphasizes security, performance, and innovation to help businesses excel in the evolving global commerce landscape. As the only company in the industry offering its services through a single unified platform, Adyen has a key competitive advantage as it doesn't have to rely on the tech infrastructure of legacy partners such as Chase Merchant Solutions, Worldpay, First Data, and Ingenico. Given its single unified platform and its global footprint, Adyen's offering is very attractive to enterprise customers. Enterprise customers like Adyen because: (1) they receive high authorization rates, (2) they can expand into new geographies quickly without additional partnerships, (3) they can see data across all channels in the same platform.

As the second largest insurance brokerage in the world, Aon is a leading global professional services firm that provides a broad range of risk, retirement, and health solutions. Aon empowers results for clients by using proprietary data and analytics to deliver insights that reduce volatility and improve performance. They operate in a somewhat non-cyclical industry that has maintained its share of GDP over time, naturally growing as business activity grows. Additionally, there is some measure of built-in inflation protection because as inflations rises, so do premiums and the fees they collect on those premiums. As a result of its virtually unrivaled global network of insurance buyers, sellers, and knowledgeable brokers, Aon is well positioned to maintain its pricing power and act as a toll taker on global insurance activity. We believe that Aon is well positioned to benefit as the insurance industry evolves its product offering to protect companies and individuals from various global trends including climate change, cybersecurity, and business interruption (pandemics, wars, etc.).

Hannover Re is one of the top global reinsurance companies with diversified exposures in property & casualty, and life & health reinsurance. Hannover Re is solely focused on reinsurance, which is essentially insurance for insurance companies. This is somewhat unique given that the vast majority of its peers also act as primary carriers. The company has a very conservative underwriting approach and also enjoys a very low-cost base. Although Hannover Re does not sport the lowest combined ratios in the industry nor does it have the highest profit margins in the industry, it is by design. The reason is that in good years, such as when pricing is strong and/or claim costs are low, management uses more of its profits to add to its reserves so that they are more insulated when the cycle turns against them. Therefore, Hannover Re has demonstrated industry low variability in return on equity and return on invested capital, while generating consistent growth in its tangible book value and its dividend.

Publicis is the world's second-largest communications group with operations in more than 100 countries. Through a series of acquisitions, the company has transitioned from a traditional advertising agency into a complete solutions provider with digital offerings and other services such as consulting. This transition has benefitted Publicis given its clients have been allocating more advertising dollars towards targeted, digital campaigns. Through its acquisition of Epsilon in 2019, Publicis significantly enhanced its data-driven marketing capabilities. This has improved the company's competitive positioning and has enabled Publicis to help its clients navigate an increasingly disruptive landscape. By improving its capabilities and competitive positioning, Publicis has been gaining market share from its peers over the last few years and we expect this trend to continue.

Reply is an IT services company that specialises in helping its customers understand and implement new technology and innovation. It offers end-to-end services from design, through to implementation, as well as operations and maintenance. The company is highly focused on niche areas within technology applications and helps its clients as they adopt artificial intelligence, big data, cloud computing, digital media, and the Internet of Things. The company operates a decentralized model that consists of 210 highly specialised companies, that are run autonomously. Reply focuses on customers across a range of sectors including Automotive, Energy & Utilities, Financial Institutions, Government & Healthcare, Logistics, Manufacturing, Retail & Luxury and Telco & Media.

Sony Group is based in Japan and is a diversified entertainment and technology company with operations spanning 5 divisions. These divisions include Game & Network Services (GNS); Image & Sensing Solutions (ISS); Music; Pictures; and Entertainment, Technology & Services. The company has leading market positions in attractive end markets with secular growth. Their Game & Network Services division revolves around the Playstation 5 console the continued release of 1st party software titles, which should expand margins in this segment. The Image & Sensing Solutions division benefits from an increase in high-end cameras for mobile phones, where they hold #1 market share. Sony is also looking to expand aggressively into automobiles. The music business has a strong recurring revenue type model and Sony is the #2 player globally across recorded and published music. They are also working to integrate their media assets and leverage their intellectual property from games to Pictures/TV which should help drive incremental profit. We are excited about the long-term prospects for the company given its strong market positions in attractive growth areas combined with a solid balance sheet.

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