NATIONAL BANK OF CANADA
FINANCIAL MARKETS

June 2025

Ottawa Pledges to Make Canada Investable Again (MCIA)

By Stéfane Marion & Matthieu Arseneau

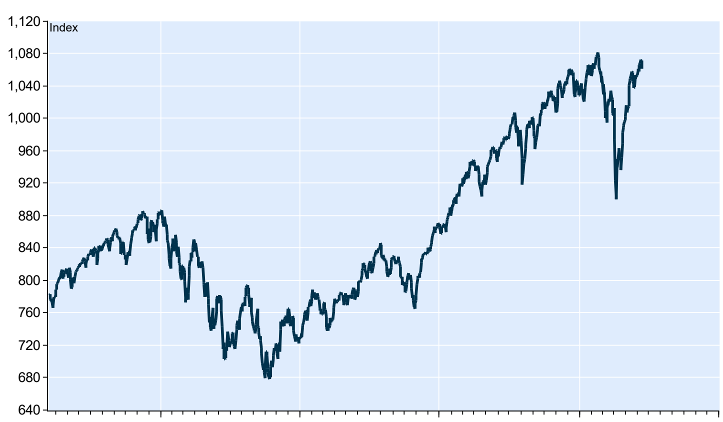
Highlights

- As if the geopolitical backdrop weren't complicated enough, the prospect of a protracted armed conflict between Israel and Iran is reviving fears of a global oil supply shock. At the same time, protectionism continues to cloud the outlook for profits. The 90-day tariff reprieve expires on July 9th, and unless a new agreement is reached, the U.S. administration is expected to impose unilateral tariff rates on key trading partners. Stagflationary pressures still pose a risk to most global equity markets.
- The S&P 500 has rebounded in recent weeks but remains below its February 2025 record high. Although the effective tariff rate has eased from its April 5 "Liberation Day" peak of over 30%, it still exceeds 14%—a level that continues to squeeze profit margins and adds to inflationary pressures. At the same time, long-term government bond yields remain elevated amid persistent fiscal concerns, creating a headwind for equity valuations—especially with the equity risk premium now virtually nonexistent.
- Despite a lackluster economic backdrop, the Canadian equity market has shown notable resilience, with the S&P/TSX up 6.4% so far in Q2 and reaching a new record high in June. The index is gaining momentum as Ottawa's latest Throne Speech marks a clear departure from the Trudeau-era approach—positioning Canada to better attract private capital. In our opinion, MCIA argues for a reduction in the S&P/TSX's valuation discount relative to the S&P 500.
- This month, we are modestly reducing our equity underweight by trimming fixed income and moving Canadian equities to an overweight position. This adjustment reflects growing anticipation of more favourable Canada–U.S. trade developments, as signaled by President Trump during the G7 meeting in Alberta. That said, our overall investment posture remains defensive as we await greater clarity on both trade tensions and geopolitical conflict.

World: Rallying through risk

Global equities have largely shrugged off the wave of pessimism sparked in April by the White House's announcement of sweeping tariffs on nearly all major trading partners. As of this writing, the MSCI ACWI has nearly recovered all losses incurred since February (see chart).

World: Global equities are rebounding
MSCI ACWI (as of June 13)



NBC Economics and Strategy (data via Refinitiv)

So far in Q2, the global equity benchmark is up 5.8% with all of the main regions showing positive growth (table).

World: All regions posting gains so far in Q2
MSCI ACWI percentage price return

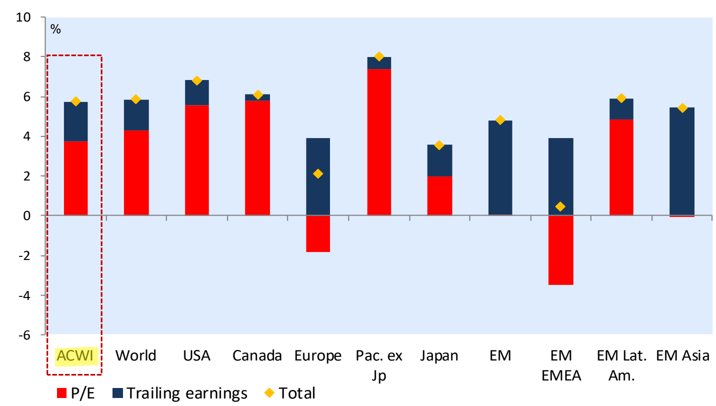
	Month to date	Quarter to date	Year to date
MSCI ACWI	0.9	5.8	3.1
MSCI World	0.7	5.9	2.7
MSCI USA	1.1	6.8	1.7
MSCI Canada	0.9	6.1	6.8
MSCI Europe	-0.3	2.1	7.8
MSCI Pacific ex Jp	1.5	8.0	6.8
MSCI Japan	-1.9	3.6	-2.0
MSCI EM	2.4	4.8	7.0
MSCI EM EMEA	-0.1	0.4	6.4
MSCI EM Latin America	0.2	5.9	12.4
MSCI EM Asia	3.0	5.4	6.7

6/13/2025

NBF Economics and Strategy (data via Refinitiv)

Roughly two-thirds of the MSCI ACWI's gains so far in Q2 have been driven by multiple expansion rather than earnings growth. In fact, only Europe and select emerging markets—namely EM Asia and EM EMEA—have posted equity gains that were not primarily fueled by rising valuations (chart).

MSCI ACWI: PE expansion at the core of Q2 rally
Breakdown of equity-market return (quarter-to-date)



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On the earnings front, corporate EPS growth expectations remain positive, with the MSCI ACWI still expected to expand 10% over the next 12 months. However, guidance continues to be revised downward, and the current pace of downgrades is the steepest since 2023 (see chart).

World: Downward revisions to earnings guidance persist
3-month change in 12-month EPS for the MSCI ACWI

NBC Economics and Strategy (data via Refinitiv)

The on-again, off-again nature of tariff threats from Washington is likely to fuel earnings volatility in the months ahead, as companies adjust inventories and navigate an increasingly uncertain business environment. The 90-day tariff reprieve expires on July 9th, and absent a new agreement, the U.S. administration is expected to impose unilateral tariffs on key trading partners. This could prompt retaliatory measures—such as further Chinese restrictions on critical exports like industrial magnets—adding pressure to global supply chains. Meanwhile, the escalating risk of a prolonged conflict between Israel and Iran is reviving fears of a global oil supply shock. Against this backdrop, stagflationary pressures remain a significant risk to most global equity markets.

World: Oil prices climb amid escalating Middle East tensions
Price of Brent oil

NBC Economics and Strategy (data via Refinitiv)

S&P 500: How high is too high for PE?

The S&P 500 has outpaced the global equity benchmark with a 6.8% gain so far in Q2. However, market breadth remains unimpressive: five of the index's ten major sectors have posted either declines (Energy, Health Care, Real Estate) or flat performance (Financials and Consumer Staples)—see table.

S&P 500: Narrow leadership behind Q2 rally
Price returns (in %)

	Month to date	Quarter to date	Year to date
S&P 500	1.1	6.5	1.6
ENERGY	8.0	-6.5	2.2
IT	2.9	15.8	1.0
HEALTH CARE	2.5	-7.0	-1.4
TELECOM	2.3	12.9	5.6
MATERIALS	0.9	1.4	3.8
INDUSTRIALS	-0.2	8.5	8.0
REAL ESTATE	-0.5	-0.7	1.9
CONS. DISC.	-0.6	8.4	-6.7
UTILITIES	-0.8	2.5	6.8
FINANCIALS	-2.0	0.0	3.1
CONS. STAP.	-2.7	0.0	4.6

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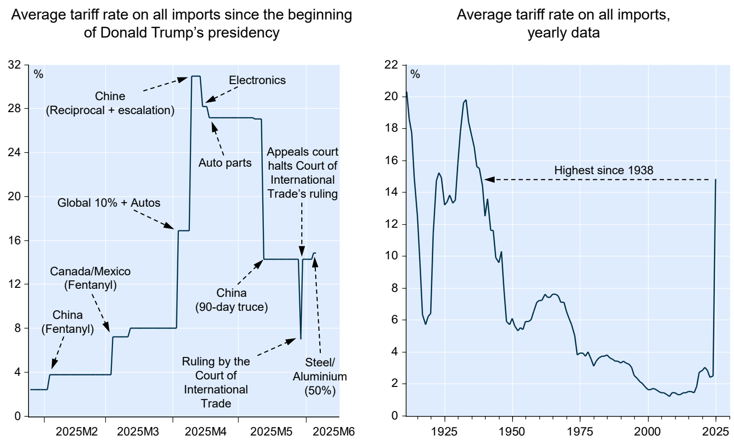
NBF Economics and Strategy (data via Refinitiv)

Tariff uncertainty remains a key drag for sentiment, undermining business confidence. Despite recent signs of de-escalation, the average duty on American imports is still expected to rise sharply in 2025—raising input costs for manufacturers and threatening corporate margins (see chart).

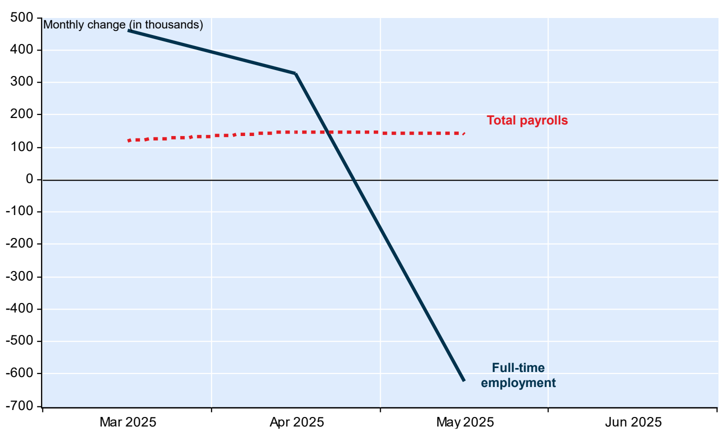
U.S. : Tariff remains elevated even after de-escalation



NBC Economics and Strategy (data via the Tax Foundation and NBC calculations)

Amid heightened uncertainty, firms are reluctant to commit to full-time hiring—favoring flexible or temporary arrangements instead. A further decline in full-time employment would weigh on consumer spending and the broader economy (chart).

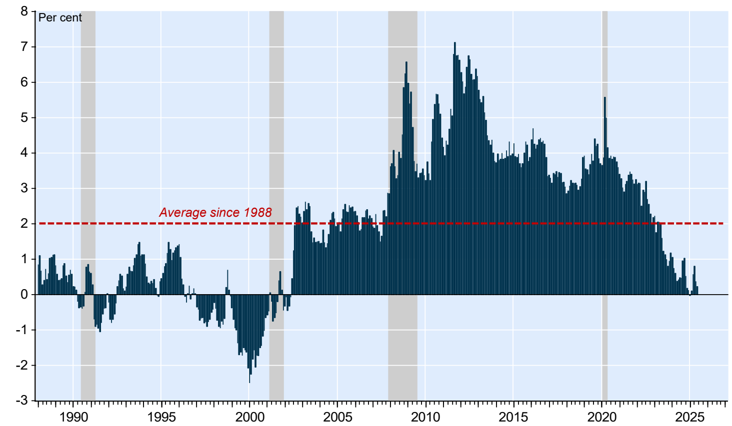
U.S.: Corporations are hiring, but not full-time
Payroll jobs and full-time employment



NBC Economics and Strategy (data via Refinitiv)

As the growth outlook softens, the stage is being set for wider fiscal deficits and limited relief from long-term interest rates, as investors demand higher term premia to lend to Uncle Sam. Despite a 21 bp decline in the 2-year Treasury yield since President Trump's election victory in November, the 30-year yield has climbed 47 bps—underscoring persistent concerns over fiscal sustainability. At the same time, multiple expansion alongside a resilient 10-year yield has effectively erased the equity risk premium on U.S. equities (see chart).

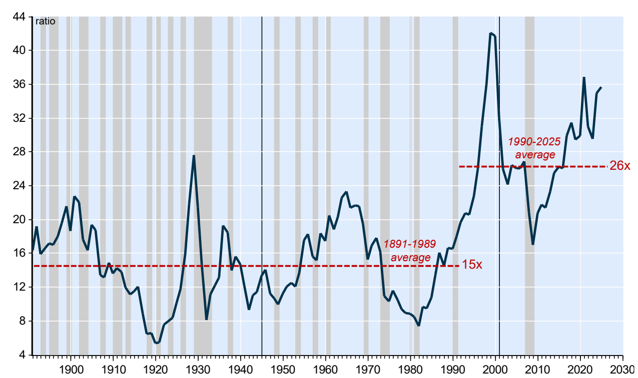
S&P 500: Equity risk premium has nearly vanished
Earnings yield less 10-year treasury yield



NBC Economics and Strategy (data via Refinitiv)

With Washington clearly intent on reshoring manufacturing to U.S. soil—potentially at the expense of foreign capital inflows—the question that naturally arises is: what is the fair PE for America's stock market? As a reminder, the S&P 500 traded at an average PE ratio of 15x earnings between 1891 and 1989. Following the fall of the Berlin Wall in 1989, as the U.S. emerged as the world's dominant military power and embraced globalization, foreign capital flowed into U.S. markets, helping lift the average PE ratio to 26x (see chart).

U.S.: Foreign investment fueled American exceptionalism after fall of Berlin wall
Trailing PE ratio for the S&P 500



NBC Economics and Strategy (data via Shiller)

This surge in global investor demand contributed to U.S. equities reaching an outsized share of the MSCI ACWI, with the U.S. eventually accounting for a staggering 63% of the global equity benchmark. Looking ahead, the shift toward repatriating industrial activity via protectionism could mean less productivity and profitability down the road (direct impact of tariffs and retaliation/boycott fro trade partners). This suggests that the fair value PE for the S&P 500 will likely be lower than the 1990–2025 average in a new world order. By how much, however, remains an open question.

S&P/TSX: MCIA propels index to record

Despite sluggish domestic demand, a soft labour market, and record-high uncertainty surrounding trade policy, the S&P/TSX surged to a new record high in June (see chart).

Canada: S&P/TSX hits new record in June
S&P/TSX

NBC Economics and Strategy (data via Refinitiv)

The Canadian benchmark is already up 6.4% in Q2. Impressively—and in contrast to the S&P 500—the gains have been broad-based, with all major sectors except Health Care posting positive returns (see table).

S&P/TSX: Gains are widespread in Q2
Price returns (in %)

	Month to date	Quarter to date	Year to date
S&P TSX	1.3	6.4	7.2
ENERGY	5.7	3.1	4.6
MATERIALS	5.7	10.0	31.9
HEALTH CARE	4.2	-2.2	-11.5
CONS. DISC.	2.4	12.3	11.5
TELECOM	0.8	0.4	0.5
REAL ESTATE	0.7	3.5	0.9
UTILITIES	0.2	4.0	7.9
BANKS	0.0	9.2	5.3
FINANCIALS	-0.4	7.1	4.7
CONS. STAP.	-0.8	5.8	4.9
INDUSTRIALS	-1.4	6.2	3.8
IT	-2.2	6.5	-1.5

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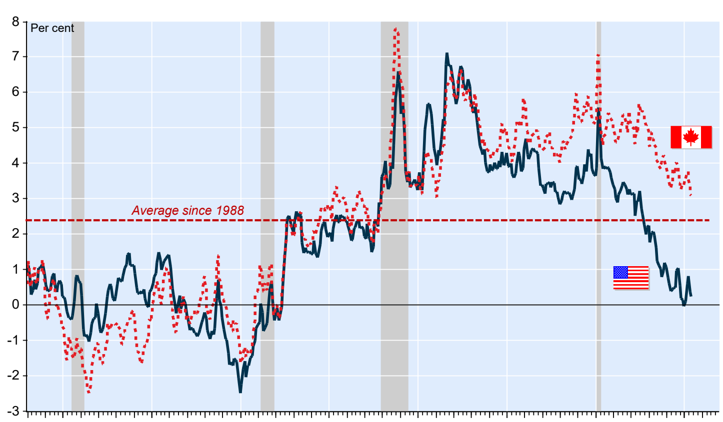
NBF Economics and Strategy (data via Refinitiv)

Despite this gain, the S&P/TSX is still offering an equity risk premium above its historical average (see chart).

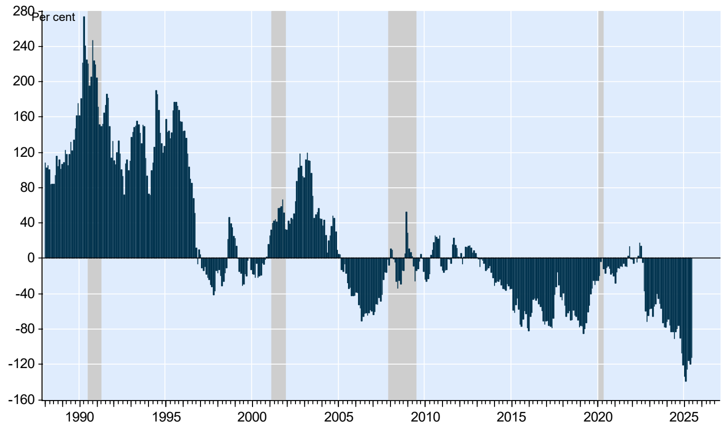
S&P/TSX: Equity risk premium still above historical average
Earnings yield less 10-year treasury yield: S&P 500 vs. S&P/TSX



NBC Economics and Strategy (data via Refinitiv)

Canada's elevated equity risk premium is partly supported by a 10-year government bond yield that remains more than 100 basis points below its U.S. counterpart (see chart).

Canada: Interest rate are well below that in the U.S.
Yield on 10-year Treasury: Canada minus the U.S.



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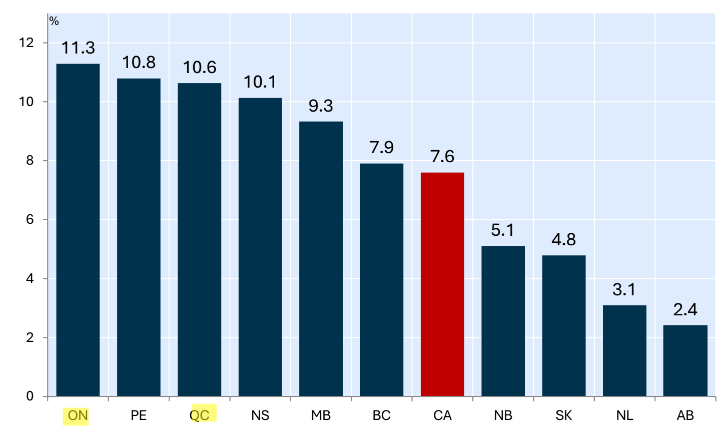
This spread reflects a weaker domestic growth outlook, softer inflation pressures, and expectations for a more accommodative monetary policy stance from the Bank of Canada relative to the Federal Reserve. The weaker growth prospects stem from the Washington's recent decision to raise import duties on Canadian aluminum and steel exports has pushed the effective tariff rate on Ontario and Quebec above 10% (see chart).

Canada: Tariff exposures vary by province
U.S. effective tariff rate on Canada and the provinces



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So, while soft growth remains likely in the second half of 2025, the outlook for the economy—and the S&P/TSX—is not entirely bleak. For one, the renewed armed conflict between Israel and Iran has already triggered a rebound in oil prices, providing support for Canadian equities. For another, President Trump signaled at the G7 summit in Alberta that he is open to resolving trade tensions with Canada within the next 30 days. Most importantly, we believe the S&P/TSX stands to benefit structurally from Ottawa's latest Throne Speech, which marks a transformative pivot toward reindustrialization. The government's commitment to leveraging the resource sector, streamlining regulation, and overhauling military procurement represents a decisive break from the Trudeau-era policy framework (see table).

Canada: Throne speech ends Trudeau era playbook
Trudeau 2021 vs. Carney 2025: A side-by-side comparison of throne speech policy orientations

Policy Orientation	Trudeau 2021 Throne Speech	Carney 2025 Throne Speech
Economic Vision	Inclusive, post-pandemic recovery focused on clean growth and social supports.	Transformative G7-leading economy with unified national market and energy dominance.
Regulatory Reform	No major change; emphasis on climate and equity lenses in regulation.	New Major Federal Project Office to cut approval times to 2 years; 'one project, one review'.
Energy Strategy	Cap oil & gas emissions; invest in clean tech and net-zero electricity.	Expand conventional & clean energy; aim to be global energy superpower.
Housing & Affordability	Childcare and rental support emphasized; Housing Accelerator Fund launched.	Double housing construction; GST cuts; Build Canada Homes agency.
Indigenous Participation	Focus on reconciliation; no major economic ownership initiatives.	Double Indigenous Loan Guarantee to $10B; enable ownership in major projects.
Trade Policy	Global trade openness and immigration-led growth emphasized.	Reduce U.S. dependence; build coalitions with like-minded democracies.
Fiscal Policy	Targeted support during pandemic; gradual spending restraint.	Cap spending growth under 2%; balance operating budget in 3 years.
Internal Market	No direct mention of internal trade or mobility barriers.	Remove federal internal trade barriers by Canada Day; $200B productivity gain targeted.
Innovation & Industry Policy	Climate innovation, clean tech manufacturing and zero-emission vehicles.	Massive industrial strategy to drive trades, science, and global innovation leadership.
Immigration Policy	Increase immigration; support family reunification; refugee resettlement leadership.	Cap temporary foreign workers and international students to <5% of population by 2027; restore trust and balance.

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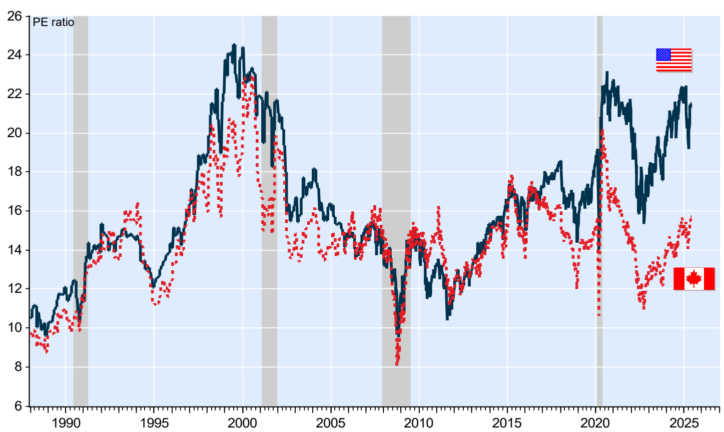
We interpret the Throne Speech as Ottawa's pledge to Make Canada Investable Again (MCIA). After years of trading at a discount to the U.S.—both at the index level and across most industries—the MCIA initiative aims to reposition Canada as a more attractive destination for both domestic and foreign private capital. In our view, this supports a narrowing of the S&P/TSX's valuation gap relative to the S&P 500 (see chart).

S&P/TSX: MCIA set to shrink the valuation gap
12-month forward PE: S&P 500 vs S&P/TSX



NBC Economics and Strategy (data via Refinitiv)

Asset allocation

This month, we are modestly reducing our equity underweight by trimming fixed income and moving Canadian equities to an overweight position. This adjustment reflects growing anticipation of more favourable Canada–U.S. trade developments, as signaled by President Trump during the G7 meeting in Alberta. That said, our overall investment posture remains defensive as we await greater clarity on both trade tensions and geopolitical conflict.

NBC Asset Allocation	Benchmark (%)	NBF Recommendation (%)	Change (pp)
Equities			
Canadian Equities	20	21	+3
U.S. Equities	20	15	
Foreign Equities (EAFE)	5	3	
Emerging markets	5	3	
Fixed Income	45	50	-3
Cash	5	8	
Total	100	100	

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Sector rotation

We have adjusted our sector positioning this month in response to a rapidly evolving environment. Given the persistence of stagflationary pressures, we expect limited interest rate relief at the long end of the curve. As a result, we are reducing our exposure to Utilities and Communication Services from overweight to market weight. In the case of Communication Services, a weak demographic outlook also contributed to the downgrade, which prompted us to lower Consumer Staples from overweight to underweight as well. Conversely, we are upgrading both Energy and Industrials to overweight—reflecting Ottawa's renewed commitment to resource development and reindustrialization. Energy was previously at market weight, while Industrials were underweight.

NBC Market Forecasts

NBC Market Forecast *Canada*			
		Actual	*Q4 2025*
Index Level		**Jun-16-25**	*Target*
S&P/TSX		26,569	25,800
Assumptions			Q4 2025
Level:	Earnings *	1517	1550
	Dividend	732	748
PE Trailing (implied)		17.5	16.6

** Before extraordinary items, source Thomson*

NBC Economics and Strategy (data via Refinitiv)

NBC Market Forecast *United States*			
		Actual	*Q4 2025*
Index Level		**Jun-16-25**	*Target*
S&P 500		6,033	5,700
Assumptions			Q4 2025
Level:	Earnings *	250	249
	Dividend	76	76
PE Trailing (implied)		24.2	22.9

** S&P operating earnings, bottom up.*

NBC Fundamental Sector Rotation – June 2025

Name (Sector/Industry)	Recommendation	S&P/TSX weight
Energy	**Overweight**	**16.5%**
Energy Equipment & Services	Overweight	0.2%
Oil, Gas & Consumable Fuels	Overweight	16.3%
Materials	**Market Weight**	**14.0%**
Chemicals	Underweight	1.2%
Containers & Packaging	Market Weight	0.4%
Metals & Mining *	Market Weight	12.1%
Gold	Overweight	9.5%
Paper & Forest Products	Market Weight	0.3%
Industrials	**Overweight**	**12.2%**
Capital Goods	Overweight	3.3%
Commercial & Professional Services	Market Weight	3.6%
Transportation	Overweight	5.4%
Consumer Discretionary	**Underweight**	**3.4%**
Automobiles & Components	Market Weight	0.4%
Consumer Durables & Apparel	Underweight	0.3%
Consumer Services	Underweight	0.8%
Retailing	Underweight	1.9%
Consumer Staples	**Underweight**	**3.8%**
Food & Staples Retailing	Underweight	3.5%
Food, Beverage & Tobacco	Underweight	0.3%
Health Care	**Market Weight**	**0.2%**
Health Care Equipment & Services	Market Weight	0.2%
Pharmaceuticals, Biotechnology & Life Sciences	Market Weight	0.1%
Financials	**Market Weight**	**32.5%**
Banks	Market Weight	20.1%
Diversified Financials	Market Weight	4.6%
Insurance	Market Weight	7.8%
Information Technology	**Market Weight**	**9.5%**
Telecommunication Services	**Market Weight**	**2.2%**
Utilities	**Market Weight**	**3.8%**
Real Estate	**Underweight**	**1.8%**

** Metals & Mining excluding the Gold Sub-Industry for the recommendation.*

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