Tariffs Shake Markets
NAVIGATING TRADE UNCERTAINTY

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What Happened?

The April 2 U.S. tariffs announcement was a "known unknown"; while we knew in advance that President Trump would reveal his plan, the details were the unknown part. Investors had been preparing for some level of damage, with the S&P 500 Index falling 8% from its February 19, 2025 high to the market close just before the announcement. It was widely expected that the news wouldn't be as bad as feared, and that the risk had already been "priced in." Unfortunately, the details turned out to be worse than expected, with generally higher rates and more countries affected.

As with any negotiation, the first offer is rarely the best offer. While we expect a worst-case scenario to be avoided eventually— meaning that tariff rates could be renegotiated between the U.S. and the affected countries — markets are now inclined to assume that the worst is the reality. The worst-case scenario could mean a weakened global economy and potentially higher inflation.

Is a Larger Market Decline Normal?

Yes, market declines within a cycle are normal. People, even a country's President make mistakes, and sometimes unforeseen events shake up the situation. The world faces challenges but always recovers being stronger. In my career, I've witnessed worse situations, including the bursting of the dot-com bubble in 2000, the global financial crisis in 2008, the Brexit in 2016, COVID-19 in 2020, and the U.S. regional banking crisis in 2023. Each of these events eventually created opportunities for future outsized returns.

What Did You Do Ahead of the Event?

It's challenging to predict what the market will find acceptable. For example, yesterday, the Wall Street Journal reported a possible 10% tariff, and markets responded with an over 1% gain minutes before President Trump announced his plan. We honestly wouldn't call a 10% tariff good news but the announcement itself turned out to be worse than anticipated causing markets to turn from positive to negative instantly.

Ahead of the event, we assumed President Trump would be fair, and we didn't take a negative view. The economy and corporate earnings had been growing strongly since 2022, continuing into 2025. The central bank had a bias toward cutting rates as inflation consistently fell. In such a backdrop, getting defensive would likely have left us "uninvested" most of the time. However, we didn't want to take the risk — even if low probability — of something unpleasant to happen. So, we bought put options for downside protection. This allowed us to participate in the upside while limiting downside risk, although with an associated cost. Given the cost, it's not something we incorporate into our portfolio on a continual basis, and it also cannot be 100%.

So, How Did We Do Today with the S&P 500 Index Falling Over 4%?

No investor should focus on a single day's performance, and we don't want to fall into the habit of analyzing short-term results. That being said, the put option strategy worked as expected, providing value. Unlike other crises where the U.S. dollar usually appreciates, the USD fell against the Canadian dollar and other currencies. We had hedged some of our

USD exposure, which added value. Our longer-term investments in growth stocks, however, were impacted as investors sold off the largest and most liquid companies, often overlooking their solid balance sheets and earnings potential. We are confident that this will correct in due time.

What Are the Catalysts for the Sentiment to Change?

If you're hoping for a quick rebound, we'll need President Trump to "cooperate". As we mentioned, what was announced likely represents the worst-case scenario, leaving room for negotiation. The reality is that Trump is looking for revenue, and some tariffs will likely remain permanent. Markets will probably accept a maximum tariff rate of 10%, which seems to be the current baseline. A more manageable outcome would encourage investors to refocus on long-term company fundamentals.

In the meantime, expect some volatility, but don't overanalyze it. If we could, we'd "fast forward" through this uncertainty, but we have a duty to monitor the situation and act accordingly. There will be new winners, and new losers.

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GLOSSARY OF TERMS

Derivatives: A financial security with a value that is reliant upon, or derived from, an underlying asset or group of assets. The derivative itself is a contract between two or more parties based upon the asset or assets. Its price is determined by fluctuations in the underlying asset.

Standard Deviation: A measure of risk in terms of the volatility of returns. It represents the historical level of volatility in returns over set periods. A lower standard deviation means the returns have historically been less volatile and vice-versa. Historical volatility may not be indicative of future volatility

Volatility: Measures how much the price of a security, derivative, or index fluctuates. The most commonly used measure of volatility when it comes to investment funds is standard deviation.

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