

Pandora's box is now open

After a rather favorable start to the year, investors were quickly thrust into a pronounced regime of uncertainty, forced to contend simultaneously with significant disruptions on both the technological and geopolitical fronts. This environment has led to a marked increase in volatility across all financial markets—equities, bonds, currencies, and commodities—even though, at this stage, the damage observed remains relatively limited in light of the solid gains recorded in 2025.

While advances in artificial intelligence have raised legitimate questions for a number of companies that have historically benefited from substantial barriers to entry, the critical issue at present remains the near-total halt of maritime traffic at the exit of the Persian Gulf—by far the most decisive bottleneck for global energy flows.

At first glance, the latest economic data remained broadly aligned with our outlook. Corporate earnings growth has largely surprised to the upside, while the labor market has remained resilient, with a relatively stable unemployment rate, inflation showing no notable excesses, and central banks still lacking any urgency to alter their monetary policy. However, the generalized shock currently observed in commodity prices is materially altering the outlook and, more importantly, the balance of risks.

More specifically, while our base-case scenario continues to anticipate a continuation of economic growth—provided that a gradual recovery in maritime traffic in the Persian Gulf begins within a relatively short time frame—the risk of a stagflationary shock, with more severe consequences for global growth, nonetheless remains non-negligible.

Against this backdrop, we reduced the overall risk level of our tactical asset allocation strategy during the third week of March, bringing the equity allocation back to a neutral stance, offset by an increase in exposure to bonds.

From a geographic perspective, we also reduced our allocation to Canadian equities over the course of the quarter, seeking to crystallize profits on a position that had become increasingly sensitive to a pullback in gold prices—a scenario that indeed materialized in March.

Moreover, we maintain an overweight position in emerging markets at the expense of developed markets outside North America. In both cases, reliance on energy imports represents a significant risk to growth. However, more attractive valuations and stronger earnings growth prospects in emerging markets represent a meaningful comparative advantage relative to the EAFE region.

In sum, beyond the very real short-term risks, it is worth recalling that history offers an important lesson regarding the effects of geopolitical shocks on equity markets. In the vast majority of cases, periods of financial stress have been followed by a recovery over a one-year horizon or longer. As such, while the current situation must be taken with the utmost seriousness, it remains equally essential to avoid decisions driven by emotion and to remain focused to one's investment horizon—an horizon that, for most investors, is measured not in months, but in years.

Q2 2026

Key elements and investment implications

Goldilocks
(10%)

- The rise in commodity prices reverses rapidly as the situation in the Persian Gulf stabilizes.
- The impact on inflation is short-lived, core measures gradually converge toward the 2% target.
- The labour market proves resilient, but some signs of weakness pave the way for two to three rate cuts by the Fed in 2026.
- Globally, fiscal expansion and less restrictive regulatory policies support economic growth.
- Earnings prospects remain robust, with significant investment in AI infrastructure continuing.
- A refocus on issues related to the cost of living by the U.S. administration facilitates a reduction in U.S. tariffs.

Economic implications: Real GDP growth ~2.5%, stable unemployment rate around 4%

Market implications: ↑Equities, ↓Bond yields, ↓Volatility, ↓USD

Trend growth
(60%)

- The rise in commodity prices reverses partially as maritime traffic gradually resumes in the Persian Gulf.
- Inflation exhibits high volatility, undermining hopes of a return to target in the foreseeable future.
- Rising energy prices weigh on the labour market, ultimately paving the way for one to two rate cuts by the Fed in 2026.
- Earnings expectations are slightly revised downward but remain solid.
- The U.S. administration shifts its focus back to growth-friendly policies. Trade tensions ease.

Economic implications: Real GDP growth near 2%, U.S. unemployment rate around 4.5%

Market implications: ↑Equities, ↓Bond yields, ↓Volatility, ↑USD

Stagflation
(30%)

- The rise in commodity prices accelerates amid ongoing turmoil in the Persian Gulf.
- Inflation rises, supply chains are disrupted, and economic activity is compromised.
- The Federal Reserve lags in cutting interest rates, waiting to see the extent of the damage to the job market.
- Earnings forecasts are being revised downward, while tech companies are cutting back on capital expenditures.
- The Trump administration attempts to reverse the trend with a series of fiscal measures, but the lack of predictability proves counterproductive, with bond markets concerned about a growing deficit.

Economic implications: Real GDP growth ~0%, U.S. unemployment rate above 5%

Market implications: ↓Equities, ↓Bond yields, ↑Volatility, ↑USD

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General

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