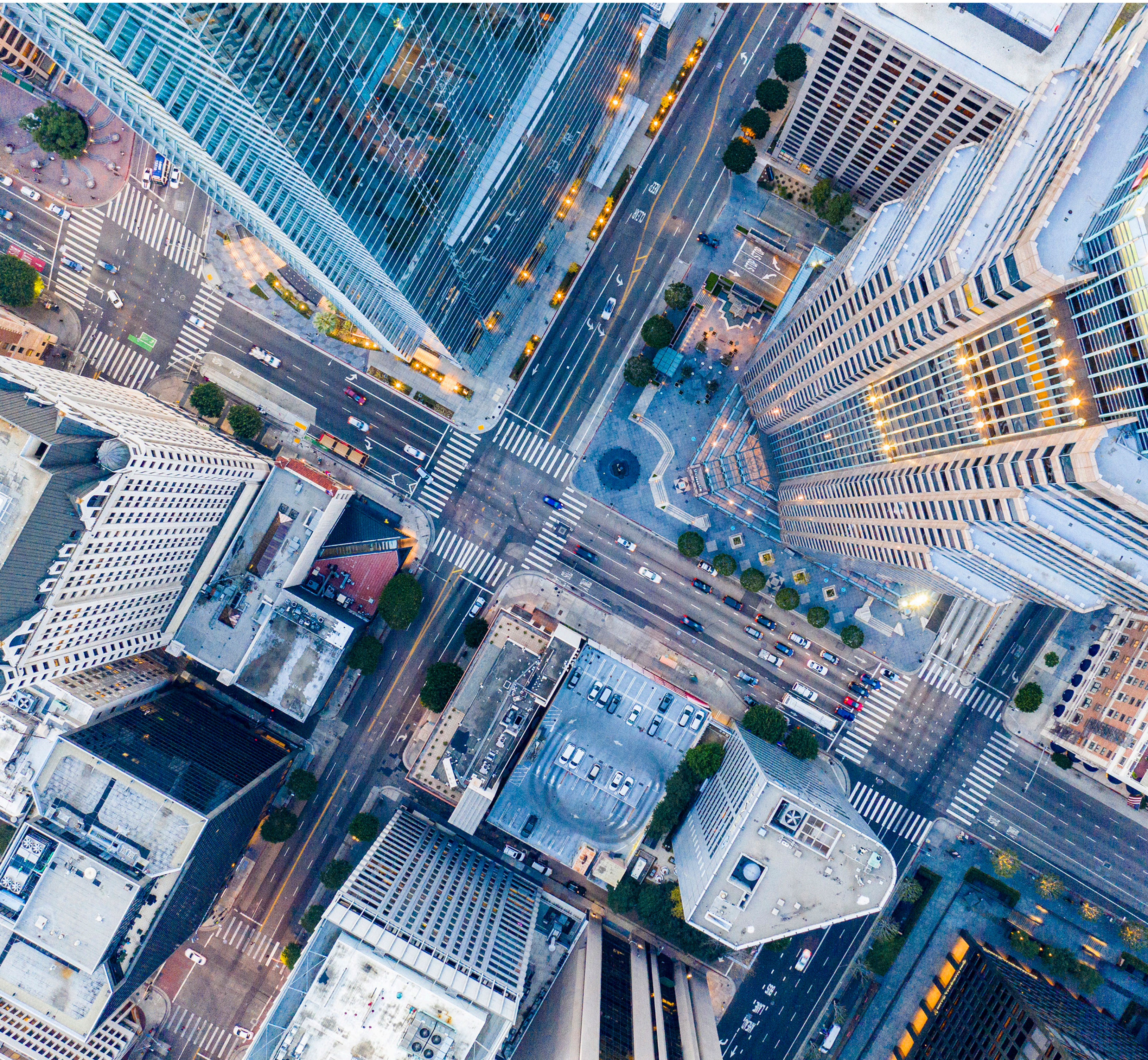
CIBC ASSET MANAGEMENT

Market Spotlight

Bond market update and Canadian equity opportunities

October 2025



As interest rates fall, fixed income investors need to focus on quality and value

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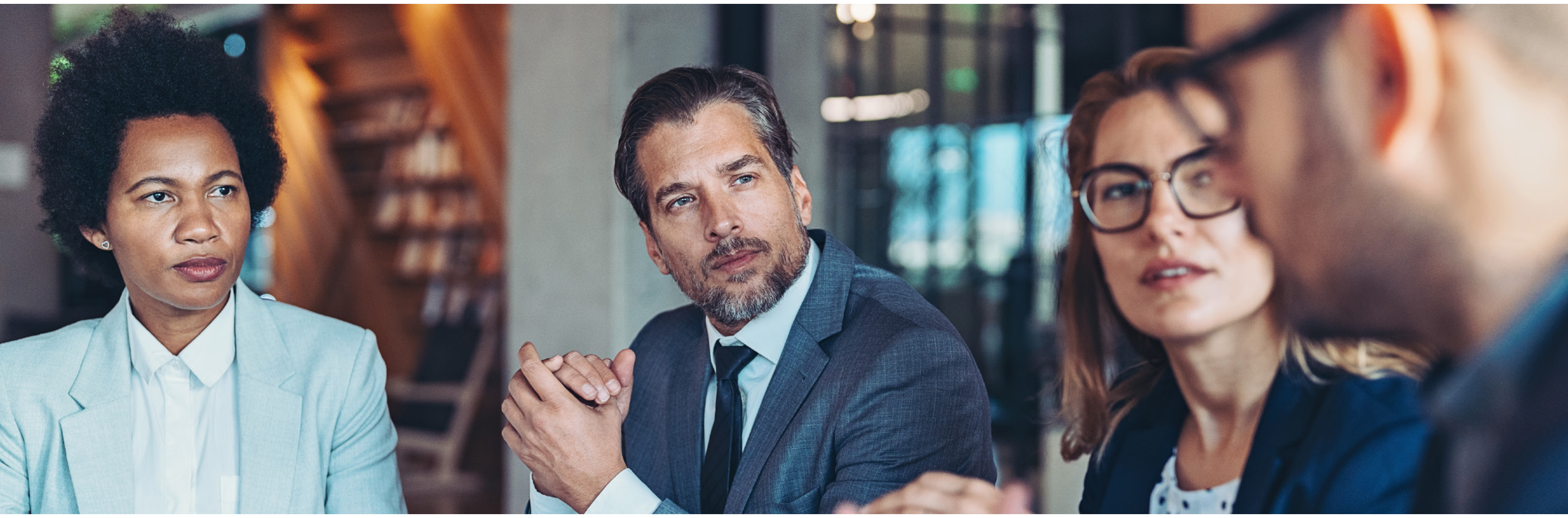

The third quarter of 2025 marked a pivotal moment for North American bond markets, as both the US Federal Reserve (Fed) and the Bank of Canada (BoC) resumed their easing cycles following a brief pause. These policy moves, widely anticipated by market participants, were a response to mounting concerns about labour market softness and economic slack, even as inflation remained above target in both countries.

Central bank policy – Easing amid uncertainty

In September, the Fed reduced its target range by 25 basis points to 4.00 – 4.25% — a move characterized as a "risk management" cut that was warranted given rising downside risks to employment, and core Personal Consumption Expenditures (PCE) inflation remaining stubbornly near 3%. The Federal Open Market Committee's (FOMC) latest projections suggest a stronger easing bias, with expectations for two more cuts by year-end, and a further cut in each of 2026 and 2027. However, the committee remains divided between those concerned about persistent inflation and those focused on labour market risks.

In Canada, the economic backdrop is more fragile. The BoC lowered its overnight rate to 2.50% amid a 1.6% GDP contraction in Q2 and a rise in unemployment to 7.1%. Wage growth has lagged inflation, and business investment remains subdued. The BoC's communications stress a data-dependent, gradual approach, with policymakers cautious about committing to a rapid series of cuts.

Market dynamics – Steepening curves and tight spreads

Yield curves in both countries have shifted meaningfully. In the US, the curve has steepened as policy easing prompted front-end yields to fall, while long-end yields remain anchored by fiscal concerns. The 10-year US Treasury yield ended the quarter at 4.13%. In Canada, the curve has normalized, with five- and ten-year government bonds yielding 2.74% and 3.17%, respectively. This normalization has improved the risk/reward profile for extending duration.

Credit markets remain buoyant, with investment-grade and high-yield spreads compressing to multi-year lows. Notably, Oracle's $18 billion USD bond issuance in September was four times oversubscribed, underscoring robust demand for yield.

Outlook – Focus on quality and relative value

Looking ahead, the economic outlook is shaped by a complex interplay of growth, inflation, and policy credibility. In the US, growth is expected to slow, and inflation is projected to remain above target before gradually easing. In Canada, recovery is likely to be slower, with the BoC maintaining a cautious approach.

Given tight credit spreads and potential market volatility, CIBC Asset Management maintains a preference for high-quality assets, prudent duration extension, and active relative value positioning — particularly in the BBB segment. Diversification, liquidity, and close monitoring of policy developments remain essential as investors navigate evolving central bank strategies and fiscal dynamics.

Oh Canada! Growth opportunities at a discount

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While Canadian investors have historically had a tendency to overinvest in Canada, this hasn't been the case with the rest of the investing world. Indeed, despite representing approximately 3% of global GDP, Canadian equities remain significantly underrepresented in many global portfolios, with fund managers allocating less than half a percent on average. Historically, this underweighting did not impede portfolio performance due to the dominance of US mega-cap technology stocks. However, recent trends signal a shift: the S&P/TSX has outperformed the S&P 500 over both one- and five-year periods on a total return basis, prompting a timely re-evaluation of Canadian equity exposure.

Shifting allocation dynamics

Over the past two decades, capital has steadily flowed out of Canadian equities as investors and pension plans sought opportunities abroad, a movement accelerated by the 2005 removal of Canada's 30% foreign content limit for RRSPs and pension plans. While this policy enabled access to global markets, the pendulum may have swung too far. Canada's market offers diversification benefits and a robust share of global GDP, positioning it as an increasingly attractive investment destination.

North America: Connected, yet distinct

Although closely linked economically, Canada and the US present distinct investment opportunities. Over 30% of TSX revenue is generated in the US, and many US companies depend on Canadian exports. TSX-listed firms benefit from low tariffs and integrated supply chains, capitalizing on US economic strength. Importantly, Canadian equities currently offer superior risk-adjusted upside, even as trade agreements like the United States-Mexico-Canada (USMCA) face renegotiation. Recent positive net inflows into Canadian equities — the first in a decade — underscore renewed global interest and momentum.

Several factors position Canadian equities for potential outperformance:

Re-valuation opportunity

Canadian equities trade at a notable discount to US peers, despite similar earnings growth and profit margins. This presents a compelling case for valuation normalization, with the S&P/TSX poised to close the gap.

Growth expectations

Consensus forecasts project low double-digit earnings growth for Canadian companies, matching US expectations. Balanced sector diversification and the rise of global champions like Shopify and Brookfield reinforce Canada's growth trajectory.

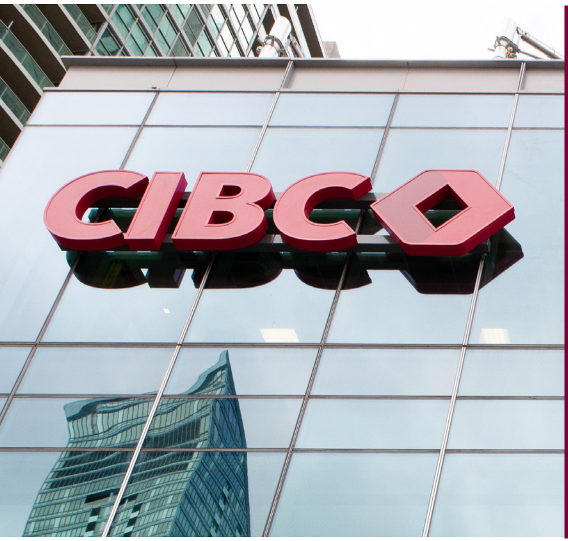
Gold exposure

The TSX's materials sector, led by gold equities, has delivered exceptional performance. Central bank gold buying and trade surpluses position gold as a major differentiator and benefit for Canadian equity holders.

Energy leadership

Canada's energy sector, including oil, gas, and uranium, offers long reserve lives and low marginal costs. With rising global electricity demand and AI-driven energy needs, Canadian producers are strategically positioned for sustained growth.

Looking ahead to 2026, Canadian equities offer compelling opportunities through attractive valuations, strong growth prospects, robust yields, and strategic commodity exposure. Recent shifts in global asset flows suggest this trend is gaining traction, presenting a timely opportunity for investors to capitalize on Canada's unique strengths.



About CIBC Asset Management

At CIBC Asset Management, we believe every customized investment solution begins with research and rigour. We specialize in a variety of investment solutions such as equities, fixed income, currency management, liability-driven investments, asset allocation and responsible investments.

Across a spectrum of investment solutions, we commit to robust research. Dedicated sector and regional analysts focus on industry research and security-specific idea generation. Our investment professionals leverage deep and diverse expertise by sharing proprietary research across asset class teams. By sharing insights across asset class teams, we maximize opportunities to add value to our client portfolios.

Contact us any time

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10/2025