CIBC ASSET MANAGEMENT

Quality in focus: The case for outperformance in 2026

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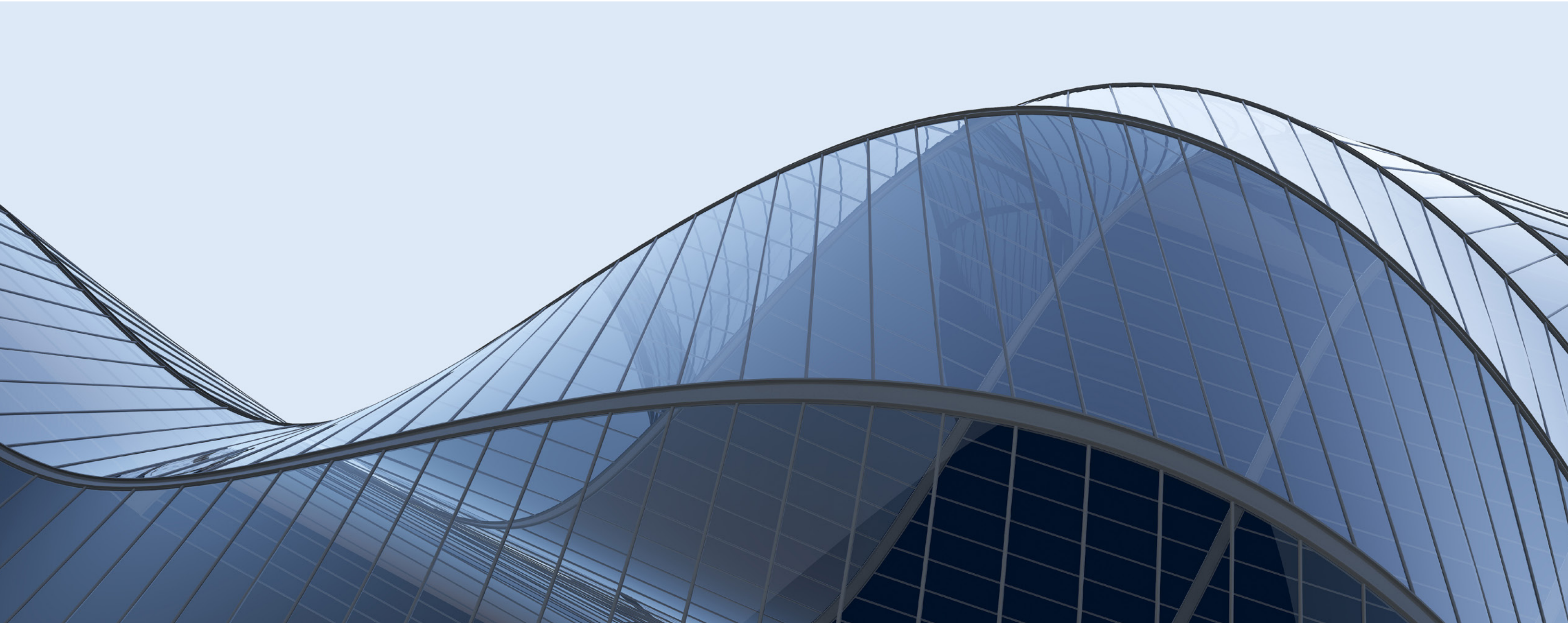
Ryan Diamant, CFA: Director – Client Portfolio Manager, Equities

With contributions from **Matthew Scherer**, CFA: Co-lead, Portfolio Manager



Executive summary

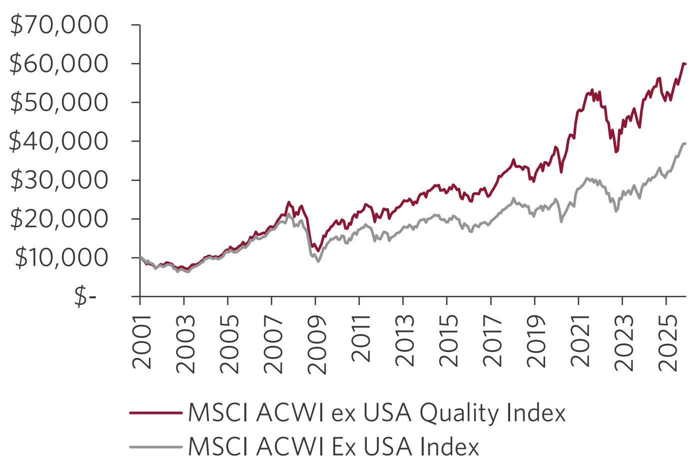
- The quality factor has outperformed the market significantly over the last 30 years.
- Quality had strong absolute performance in 2025, but lagged the market on a relative basis despite being the best-performing factor over the prior decade.
- The quality factor sold off after overvaluation, starting 2025 at the widest relative valuation premium versus the market since the pandemic.
- 2025 was the worst year for international quality relative performance in history.
- In the second half of 2024, quality traded more than +1 standard deviation above its long-term relative valuation average, indicating overvaluation.
- Following 2025's relative underperformance, the quality factor now trades around -1 standard deviation below its long-term relative valuation average and we now view the factor as attractively valued.
- For 2026, the quality factor is expected to deliver faster EPS growth than the market.
- The CIBC International Growth Strategy offers an effective way to gain access to quality as a core holding within a diversified portfolio.

International quality factor has outperformed over the last 30 years

For decades, investors have targeted certain quantifiable characteristics or "factors" to seek long-term investment returns above their benchmarks. Common factors include quality, low volatility, size (small-cap), momentum, growth, and value, among others. Investment approaches that target the quality factor have historically outperformed. Using International (MSCI ACWI ex USA Index) and European (MSCI Europe Quality Index) quality factor indices since their respective inception dates in 2001 and 1986, the quality factor has outperformed the market by 1.82% and 1.32% annualized, as at November 30, 2025. From a portfolio construction standpoint, this has supported maintaining a strategic allocation to quality as a core factor exposure.

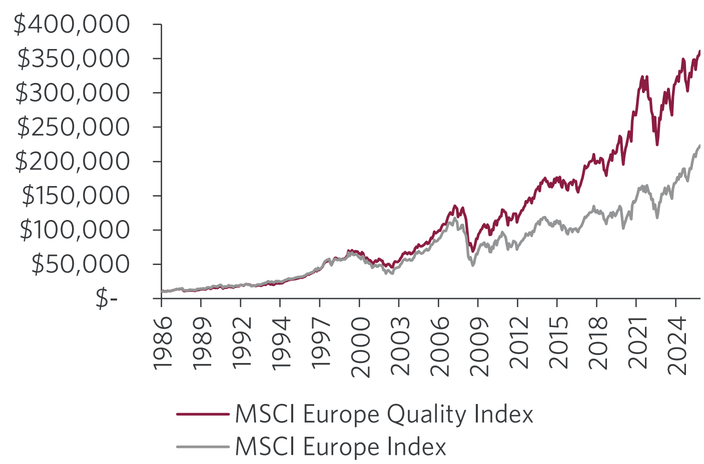
Growth of $10k: International quality vs market

Jan 1, 2001 to Nov 30, 2025



Growth of $10k: Europe quality vs market

Jan 1, 1986 to Nov 30, 2025

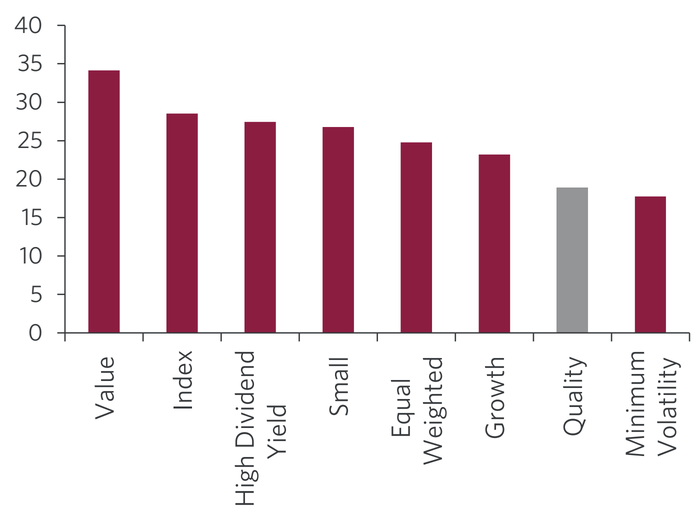


Source: Morningstar Direct, as at November 30, 2025

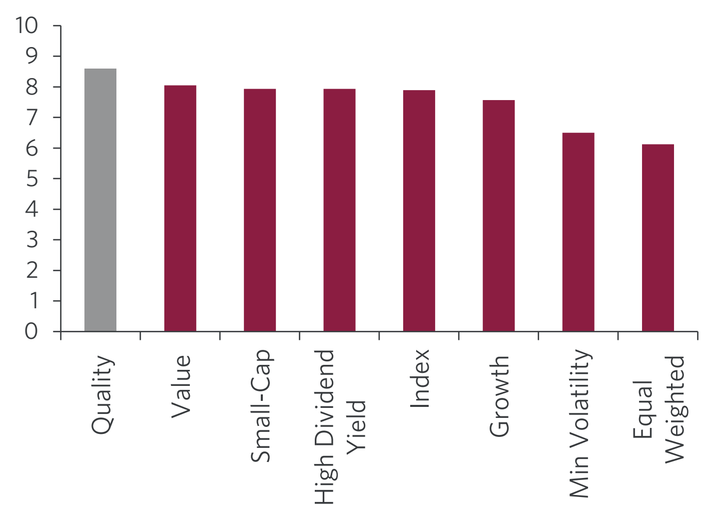
The worst year for quality in history

In 2025, the factor narrative shifted materially. Although all International factors posted double-digit absolute returns, quality lagged the market on a relative basis despite being the best-performing factor over the prior decade.

YTD returns (%) – MSCI ACWI ex USA factors



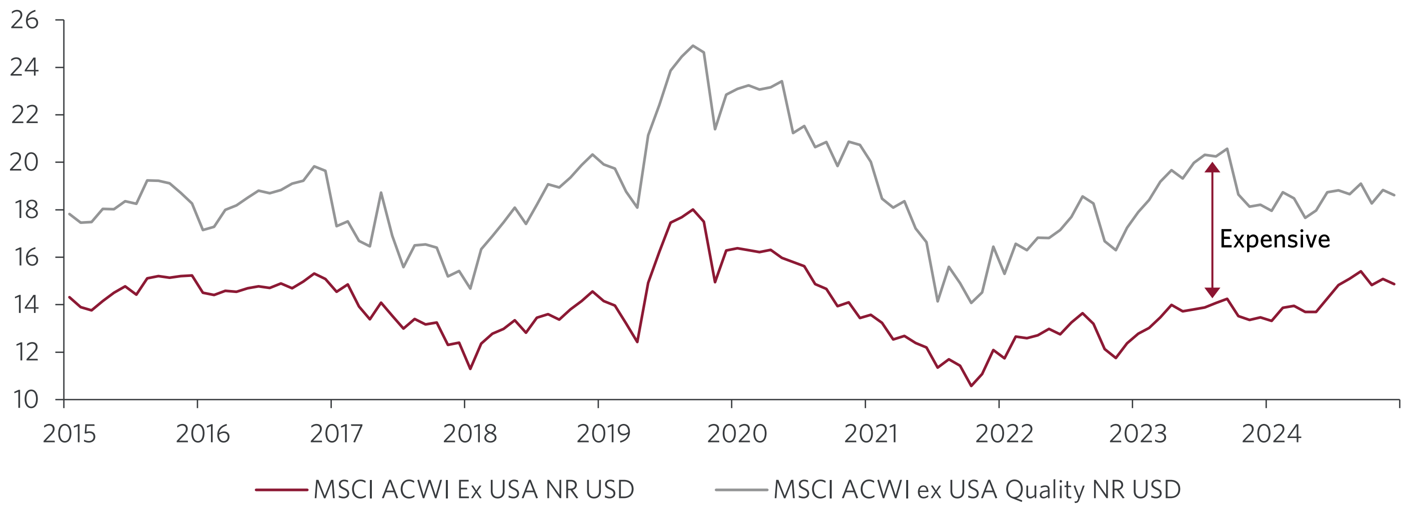
10 year returns (%) – MSCI ACWI ex USA factors



Source: Morningstar Direct, as at November 30, 2025

Following Liberation Day, market conditions turned more speculative, favouring lower-quality value and momentum stocks which outperformed the broader market. A cyclical earnings recovery in financials and industrials, alongside improved fundamentals in energy and materials sectors supported value stocks. As strong as momentum and value were in 2025, their outperformance partly reflected the starting-point overvaluation of quality heading into the year.

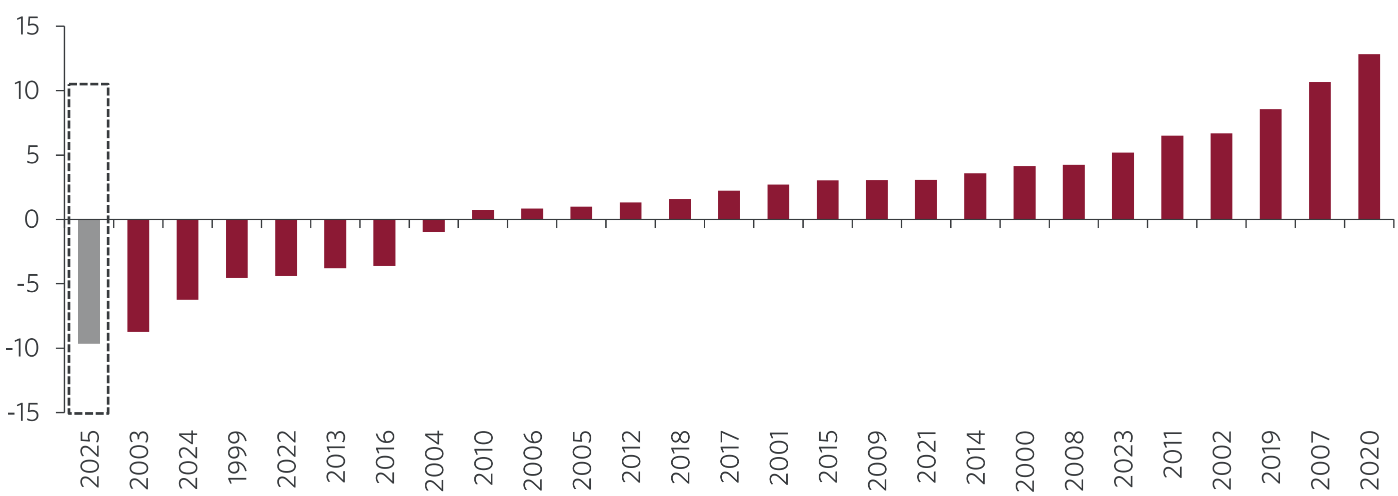
Last 10 years – Forward P/E Ratio: International Quality vs. Index



Source: Morningstar Direct, as at November 30, 2025

Quality companies typically trade at premium valuations due to strong margins and profitability, lower leverage, and high returns on invested capital. Softer attributes also support higher multiples, including capable management teams, and incentives aligned with shareholders. However, the quality factor sold off after overvaluation in the second half of 2024, trading at one of its widest relative valuation premiums versus the MSCI ACWI ex USA index since the pandemic. As we entered 2025, we observed a rotation out of higher-valuation segments and into cheaper parts of the International market. We view this rotation as cyclically justified but atypical to long-term factor behaviour. Dating back to 1999, 2025 was the worst year for international quality relative performance since index inception. Similarly in Europe, 2025 was the second-worst year for quality since the index's inception in 1987.

MSCI ACWI ex US Quality Index – MSCI ACWI ex US Index: Calendar year relative returns since inception (1999 to 2025)



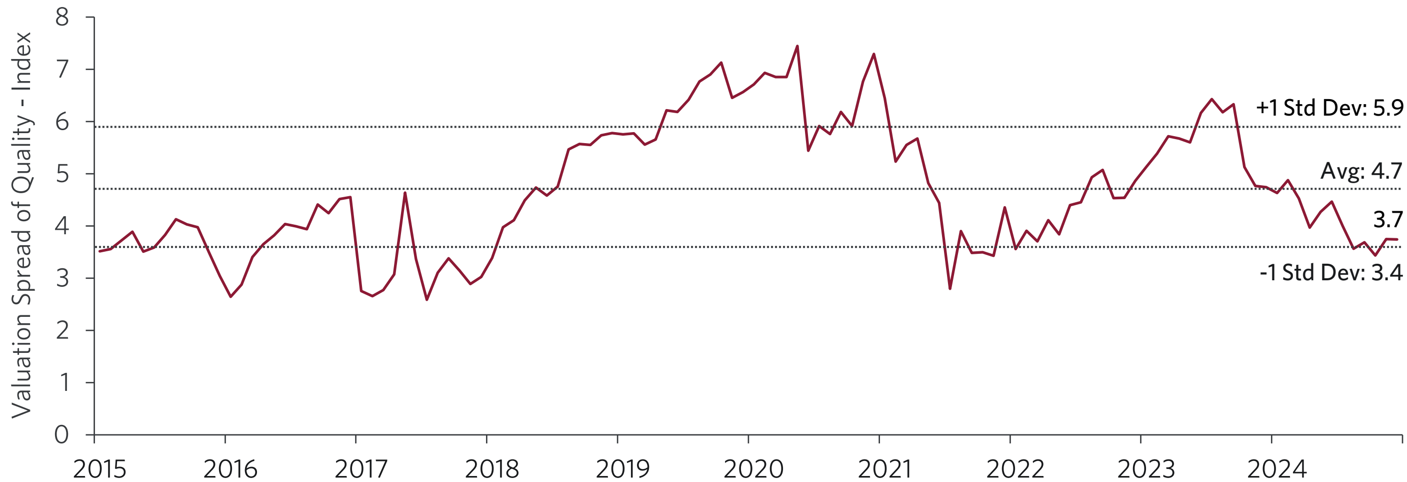
Source: Morningstar Direct, as at November 30, 2025

The quality factor is not broken but has been repriced, and we believe this positions high-quality equities for a favourable setup in 2026 and beyond.

A strong setup for 2026

Following the sell-off which began in 2024, the quality factor now trades at an attractive valuation relative to the market.

Last 10 years – Forward P/E Ratio Spread: International Quality – Index

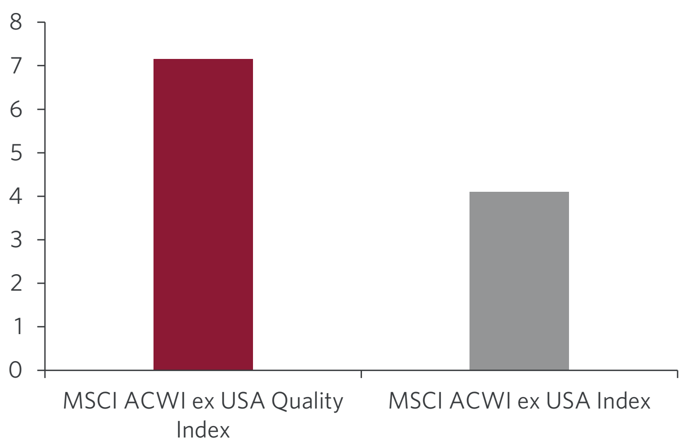


Source: Morningstar Direct, as at November 30, 2025

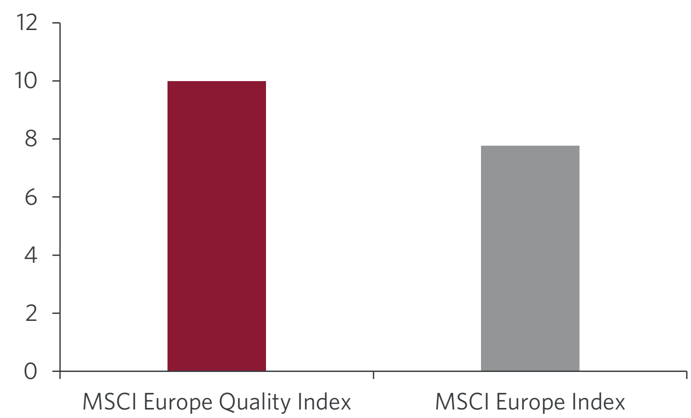
In the second half of 2024, quality traded more than +1 standard deviation above its long-term relative valuation average, indicating overvaluation. Following 2025's relative underperformance, the quality factor now trades around -1 standard deviation below its long-term relative valuation average. We view the factor as now attractively valued.

In addition to more attractive valuations, quality stocks are expected to deliver faster 2026 earnings growth than the broader market in both Europe and International markets.

EPS growth est next fiscal year (2026)



EPS growth est next fiscal year (2026)



Source: Morningstar Direct, as at November 30, 2025

Earnings per share (EPS) growth indicates whether a company is becoming more profitable over time. A rising EPS typically means the company is making more money for each share owned. For 2026, the quality factor is expected to deliver faster EPS growth than the market. This outlook is supported by multiple catalysts, including expanded European fiscal spending, increased defense expenditure amid an increasingly unstable geopolitical backdrop, technology and artificial intelligence catch-up in international markets, as well as potential deregulation that could reduce business regulatory burden. Taken together, these catalysts combined with more attractive valuations position quality well over the medium-term.

CIBC International Growth Strategy has a quality and growth bias

The CIBC International Growth Strategy is a core portfolio that invests in high-quality companies with above-average growth, trading at attractive valuations. We invest in companies with defendable and thriving business models, superior profitability, high returns on invested capital and cash-flow generation, as well as consistency. We also look for strong balance sheets and low leverage. We also draw on over 200 C-suite company meetings annually to enhance our assessment of quality across the companies we research. Given our approach, we tend to skew towards having a quality and growth bias.

As we begin 2026, we believe the quality factor is behaving consistently with historical patterns, underperforming early in risk-on recoveries with the potential to transition to relative strength as the expansion broadens and earnings visibility improves. US equity market valuations remain elevated versus historical measures, and many of the drivers that supported international equity market outperformance in 2025 versus the US persist. Valuations in international markets are relatively more attractive, and we view the setup for quality heading into 2026 as favorable for investors considering exposure. We continue to recommend quality as a core factor exposure and believe the CIBC International Growth Strategy offers an effective way to gain access within a diversified portfolio.

About the team

Daniel P. Delany, CFA, Co-Lead Portfolio Manager

Dan Delany is an equities portfolio manager with more than 20 years of industry experience. Prior to joining Geneva Advisors, which became part of CIBC in 2017, he was a portfolio manager and investment analyst at Oak Ridge Investments in Chicago. He began his investment career at Kemper Funds in 1993 and later worked for UBS AG in Europe and William Blair & Company in Chicago. Dan received his Bachelor of Arts degree in international affairs from Marquette University. He then earned his Master of Business Administration degree from Northwestern University's Kellogg School of Management and, subsequently, his Chartered Financial Analyst® designation. He is an active member of the CFA Society of Chicago and president of the School Advisory Board at the St. Norbert School in Northbrook, Illinois.

Matthew K. Scherer, CFA, Co-Lead Portfolio Manager

Matt Scherer is a portfolio manager and equities analyst with more than 20 years of industry experience. Prior to joining Geneva Advisors, which became part of CIBC in 2017, Matt was a research analyst at Aragon Global LLC, where he worked as a consumer and business services analyst. Previously, he worked in London for Carlson Capital UK as a research analyst covering European equities. He began his career with RBC Capital Markets as an associate analyst covering restaurants. Matt received his undergraduate degree from the University of Wisconsin and a Master of Business Administration degree from the University of Chicago Graduate School of Business. He also studied at the London Business School. Matt holds the Chartered Financial Analyst® certification.

Ryan Diamant, CFA, Director – Client Portfolio Manager, Equities

Ryan Diamant is a Client Portfolio Manager – Equities responsible for working with internal and external partners to develop effective investment solutions for clients, prospects and consultants. Prior to joining CIBC Asset Management in 2021, Mr. Diamant was a Senior Product Manager at Invesco Canada focusing on their global, international, and emerging market franchises. Mr. Diamant was also in the Rotational Leadership Development Program at Sun Life Financial, serving in their defined contribution and wealth management businesses. Mr. Diamant holds a Honours Bachelor of Business Administration degree from Wilfrid Laurier University. He is also a CFA charterholder and a member of the CFA Society of Toronto.

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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 insight across asset class teams, we maximize opportunities to add value to our client portfolios.

Contact us anytime

To learn more about CIBC Asset Management and our investment solutions, please contact your advisor or your CIBC representative. For more insights, connect with us on LinkedIn.

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