

WEEK ENDED MARCH 7, 2025

Carol Schleif, CFA, SASB-FSA
Chief Market Strategist

Breathe

"Between stimulus and response there is a space. In that space lies our freedom to choose our response."

- Widely attributed to Viktor Frankl, Austrian psychiatrist and holocaust survivor

The Through Line: Our natural wiring prompts us toward a desire for instant (and all-too-often hyper emotional) reaction to breaking news. Yet we are the only species blessed with the ability to pause before responding. Training ourselves to use that space to inform our decision making can help soothe short-term nerves and set the tone for wiser long-term investment decisions.

Our pesky lizard brains

Well, that was quick. We advocated in last week's [Weekly Strategy Perspectives - When the only way out is through - BMO Wealth Management](#) to "please rip the (tariff) Band-Aid off." And off it came - much to the chagrin of global capital markets. Uncertainty remains the operative word as U.S. administration officials flash conflicting signals and target countries react with actual and threatened counter measures. Investor nerves remain raw, and stomachs unsettled.

The human race has endured for millennia thanks in part to survival instincts buried deep within the most primitive parts of our brains. We seek predictability and certainty over chaos. We hang with the pack versus going it on our own. We disproportionately weight information (even more so if it is recent) that supports our beliefs while discounting anything that tells a different story. And, most pertinent this week, we fight, flee or freeze when confronted with seemingly dire emergencies. These traits are so hard coded into our most ancient wiring that those who study it (behavioral scientists) have named it our "lizard brain."

Tariff tantrum

When unexpected events hit, the almost irresistible urge is to sell first and sort details later - especially when the entire pack seems bent on reducing exposure. Markets had watched for months as tariff threats were made, only to be withdrawn at the last moment. When levies were *actually* deployed it came as a profound surprise. True, evidence of growing nervousness had been mounting for weeks:

- February's PMI report showed solid factory output, but faster than expected hikes in input prices and significant signs of goods stockpiling
- other business surveys, including the National Association of Home Builders and NFIB, illustrated surprising drops in confidence
- surveys from the Conference Board and University of Michigan produced flagging consumer sentiment scores, accompanied by slowing spending growth and higher prices

Yet equity markets had been able to largely sidestep the gathering clouds, rolling along to new highs as recently as February 19.

Funny thing happened on the way to the (stock) market

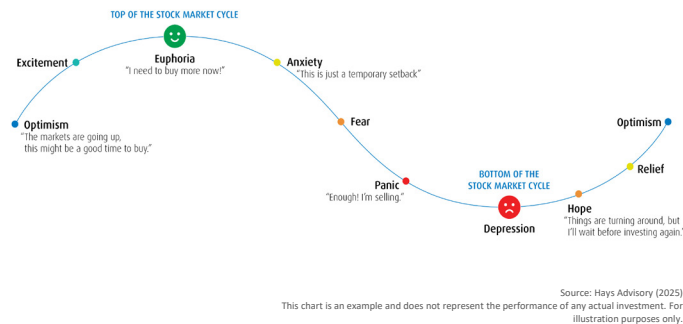
While a ton of proverbial ink and airspace is devoted daily to trying to "predict" markets, short-term trading can often be more influenced by emotions than fundamentals. Greed and fear rule the day as can technical factors such as when large algorithmic trades or rebalances occur; indexes are reconstituted; triple witching (quarterly expiration of options, futures, and options on the futures simultaneously expire forcing unwinding of trades) is scheduled; or year-end mutual fund window dressing is due.

Though headwinds and tailwinds swirl simultaneously on most days, investors have a way of putting a thumb on the sentiment scale to emphasize one side or the other depending upon the prevailing mood. When things are running well, time horizons extend, disconcerting news that doesn't support the narrative is discounted and risk-on trades are justified (AI and Mag 7

anyone?). Conversely, when the door to the worry closet opens, a whole host of things spill out, bringing the time frame of concern from “next decade” to “end of day.” Market pendulums swing from greed to fear and back again (chart 1) with amazing regularity.

Chart 1

Investing and Emotions



Fundamentals matter

While emotions might influence the short term, fundamentals ultimately drive the intermediate and longer term as corporate progress and economic realities play out. This is especially important to remember when short-term emotions have knocked markets for a loop and our defense mechanisms urge an emotional response.

Coming into 2025, the U.S. economy was on solid footing, with steady GDP growth in the 3% range, above-average productivity growth, declining inflation and unemployment levels that had hovered in the low 4% range (historically low) for several years. Corporate earnings have largely beat expectations in the last few quarters and were projected to continue that pattern for at least the next year or so.

Canada, too, was showing green shoots of optimism thanks to the Bank of Canada’s world-leading rate-cutting campaign that has started to revive the highly interest-rate-sensitive economy.

From a stock market perspective, both the S&P 500 and TSX started the year strongly, posting fresh all-time highs just weeks ago. Against this backdrop it is wise to stop, take a breath, and carefully consider if recent data is extra noisy due to corporate front running of potential tariffs or a legit change in the business environment. Similarly, are the recently announced tariffs going to stick (leading to longer-term change in the trajectory of fundamentals) or will they be rolled back, modified or adjusted for key industry, country or company exemptions?

The “Trump (tariff) put” – fact or fiction?

After two days of severe equity market declines, investors were hoping for some indication from President Donald Trump that he might find a way to quickly back down or reduce the levies applied on March 3 to core trading partners. Numerous reports in recent days have outlined the potentially dire hits to consumers, industries and countries if the tariffs remain in place for any length of time. It was hoped that President Trump’s propensity for considering stock market behavior in his self-appraisal could lead to retraction of at least a portion of the levies – the so-called “Trump put.”

During a speech to a joint session of Congress on Tuesday evening, however, President Trump reiterated his commitment to tariffs. He noted that a necessary “adjustment period” might be needed before the momentum returns, but tariffs would ultimately “make America rich again” by bringing in trillions. Interestingly, on Wednesday President Trump agreed to push auto tariffs off by a month – rallying markets strongly in the decision’s wake.

What to make of the road ahead?

Parsing short-term noise from long-term fundamental change is difficult in the best of times. It’s an especially trying task when the quantity of potential change is as vast as global investors have faced in just the last few months. Geopolitical and political upheaval, potential trade wars, new technological shifts, diverging central bank policies, shifting currency relationships and gyrating markets create cross currents and multi-level knock-on effects that are difficult to unwind.

The key is understanding that we can’t help our primitive wiring and it’s going to push us to operate from an emotional starting point, particularly when confronted with unexpected news. On the one hand, tariffs will likely not work as a revenue generator if a full-blown trade war commences and/or consumers pull back. U.S. consumers at all but the top tier have been stretched for years by price levels that, in aggregate, remain far above pre-pandemic levels. Canadian consumers, who have begun to revive only recently, are likely to go into retreat if a bruising trade war drags on. Trading partners such as China know right where to hit back. A lasting trade war benefits no one.

On the other hand (and looking longer term), shifting key manufacturing activity back to the U.S., redistributing global supply chains, spreading the cost of military spending/support and better balancing economies from lopsided dependence on consumption (U.S.) or exports (China, Germany) is theoretically a plus for the globe. But getting there is definitely not going to happen without pain and dislocation. Moving from agrarian societies to manufacturing-based economies was undoubtedly painful for makers of buggy whips and wagon wheels even as it created opportunity for new industries and innovators. In Canada, the collective anger and sense of betrayal over verbal blows as well as the trade war is uniting the country.

Implications for investors

The period we're in right now is filled with all sorts of concerns that make our lizard brains want to react from emotion. However, numerous studies point to the detrimental impacts of trying to time markets (thinking you can get all the way out and then back in). Market timing demands two correct predictions – when to sell and when to move back in – which are both difficult to time accurately. We rarely want to sell when things have worked any more than we want to buy when assets are deeply discounted. Mountains of empirical evidence show that people often become paralyzed after moving to the sidelines while active traders tend to hamper their own results by always second guessing decisions. **It's not what you make, it's what you keep.** As chart 2 illustrates, missing even the five or ten best days substantially reduces one's long term return.

Equity market declines this week were difficult but not outside the realm of typical. Mid-digit pullbacks are the norm not the exception, even in up-trending markets (charts 3 and 4). Keep in mind most U.S. and Canadian indexes are back to flat for the year (other than NASDAQ, which is down 5%). It is also worth remembering that bond or cash positions in portfolios

have provided supportive ballast, particularly as long-term yields have fallen. It's often overlooked that despite the rapidly evolving geopolitical and political headlines, many global indexes are up double digits year to date, including China and Germany.

It will likely take time for fundamentals to provide a clearer indication of which way they will ultimately break. In the meantime, a few deep breaths and a steady conversation with your investment professional can provide the necessary perspective in that space between stimulus and the response that is right for you.

Additional BMO Tariff Insights

Douglas Porter, CFA, Chief Economist BMO Financial Group
[Trade War Impact: Take Two](#)

Yung-Yu Ma, Ph. D, Chief Investment Officer,
 BMO Wealth Management – U.S. [Trade War – ACT II - BMO Wealth Management](#)

Brent Joyce, Chief Investment Strategist, BMO Private
 Investment Counsel, Inc. [BPIC March Strategy Update](#)

Chart 2
 Performance of \$1,000,000 Invested in the S&P 500®

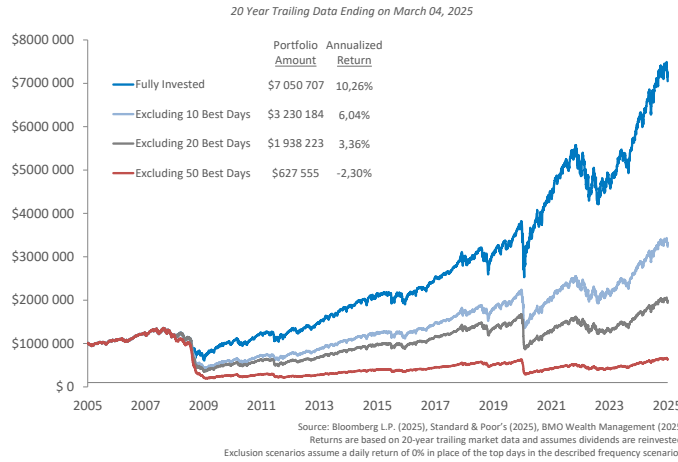


Chart 3

S&P/TSX Composite Returns & Intra-Year Pullbacks

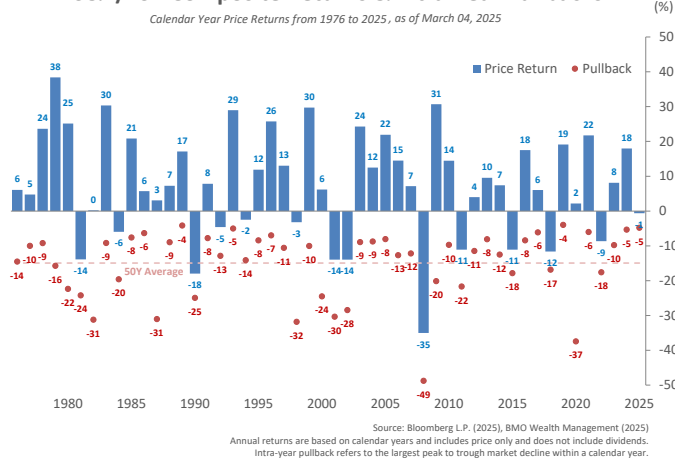
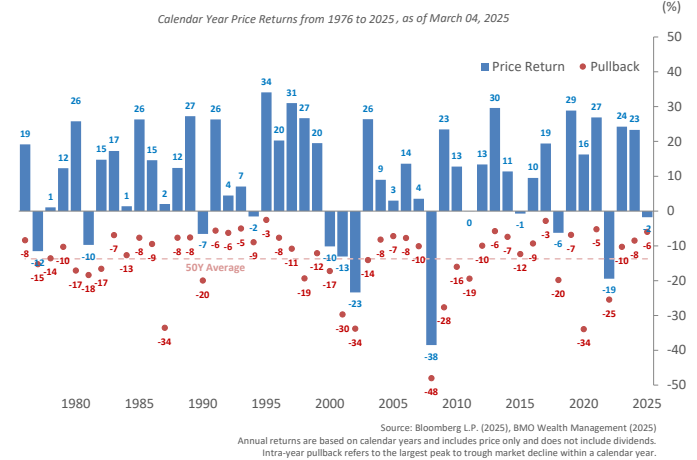


Chart 4

S&P 500 Returns & Intra-Year Pullbacks



In focus in North America

Jon Borchardt, Sr. Analyst

George Trapkov, CFA, VP and Portfolio Manager

This week

Green shoots in Canadian economic data, for now –

The Canadian economy firmed in Q4, with real GDP growth clocking in at a solid 2.6% annualized, well above consensus and the Bank of Canada's latest forecast. The strength was broad based, led by a 5.6% boost to consumer spending. Housing was solid as well, up 16.7% (the best gain in nearly four years), led by a big increase in resale activity. Even business investment joined the party: it rose 8%, driven by machinery and equipment. The January flash estimate was a solid +0.3%, with some of that likely due to front-loaded activity ahead of potential tariffs. Still, that's a good start to Q1 and 2025. **President Trump's tariff hammer will come down hard on Canada's economy. If the announced tariffs remain in place for one year, the economy faces the risk of a moderate recession.** A few quarters of contraction are well within the realm of possibility. With little confidence, given the lack of historical precedent, BMO Economics estimates that the tariffs will reduce real GDP growth by roughly 1.5 percentage points to around 0.5% in 2025. This reflects reduced demand for Canadian exports to the U.S. (which account for about a fifth of GDP); disrupted supply chains impeding business activity and consumption; and heightened uncertainty that reduces business investment.

Tariffs on key U.S. allies begin – U.S. equities sold off Tuesday morning after the government enacted 25% tariffs on Canada and Mexico, along with an additional 10% tariff on Chinese goods. **Canadian Prime Minister Justin Trudeau announced retaliatory tariffs, declaring the U.S. had started a trade war and warning it would lead to higher prices and job losses for U.S. consumers. China retaliated by pausing imports of U.S. soy and lumber while imposing tariffs on select agricultural products.** Target CEO Brian Cornell warned that fruit and vegetable prices could rise within days, as the U.S. relies on Mexican imports during winter. Best Buy CEO Corie Barry stated that vendors across the company's entire supply chain would pass along some level of tariffs, likely driving prices higher for consumers. Walmart noted that tariff worries are pressuring consumer sentiment. President Trump acknowledged the economic impact in his address to Congress, admitting that tariffs could cause "a slight disturbance" for consumers. However, within 24 hours, the administration signaled a softening stance. On Wednesday, Trump announced a one-month exemption from cross-border auto tariffs, granting temporary relief to automakers and boosting equity markets in the process. The administration now shifts focus to April 2, when reciprocal tariffs are set to take effect.

Incoming U.S. Data continue to illustrate signs of uncertainty tinged with optimism – The Institute for Supply Management (ISM) released February survey data for both the Services and Manufacturing sectors. While both sectors continue to expand, there are clouds on the horizon that warrant close monitoring. Respondents in both industries expressed rising uncertainty over trade policies and other government actions. **Cost inflation is reemerging as a headwind, with tariff threats driving a significant increase in input costs and a contraction in new orders for the manufacturing sector.** The post-election optimism seen in January's surveys has begun to wane as uncertainty over the economic and policy outlook grows. **The concerns highlighted in the ISM surveys are echoed in the Federal Reserve's February Beige Book.** Manufacturing companies surveyed by regional banks cited tariff concerns and rising costs as key challenges. The Services sector presented a mixed picture—while restaurants grew less optimistic, consulting firms reported increased business activity, driven by the changing and uncertain U.S. policy environment. **Despite these concerns, the ISM surveys indicate that firms remain generally optimistic,** holding out hope that deregulation and lower taxes will provide an impetus for improved business conditions later in the year.

Canada Bank Earnings – Banks wrapped earnings reports in the last week and delivered strong results. Canadian banking – bread and butter for the group – was solid overall. RBC led while National results were impacted by higher credit provisions. Capital ratios remain robust with some banks announcing buybacks. As economic growth expectations moderate in Canada, so will the outlook for bank earnings. This will likely pressure valuation multiples lower.

Germany announces "whatever it takes" – shock and awe proposal in rallying support for Ukraine. The realization that U.S. assistance for Ukraine and commitment to defending allies on the other side of the pond is now in question was described as a psychological shock – Europe's 9/11 moment – according to Evercore ISI Central Bank strategist Krishna Guha. Amid fears that the Trump administration is actively undermining Germany's elections, **Chancellor-to-be Friedrich Merz announced that centrist parties have come together to propose a constitutional amendment that would exempt defense spending from the national debt cap.** This move will enable the German government to significantly ramp up military expenditures. **Additionally, Mr. Merz unveiled a US\$500 billion, 10-year infrastructure investment plan, which is expected to boost manufacturing activity and act as a fiscal stimulus for the economy.** In response, German bund yields climbed higher and the euro strengthened. **Meanwhile, the European Commission is crafting a broader defense spending package, signaling a long-term shift.** Four to five years down the road, Europe could emerge as a far more self-reliant force.

Next Week

In Canada, a central bank rate decision comes on Wednesday. In the U.S., inflation and sentiment (both business and consumer) will be under the microscope again given key data releases. The U.S. congress will continue to try to hammer out a budget in order to avoid a Friday night government shutdown. Tariff machinations will remain front and center.

- **Tuesday 3/11** – U.S. NFIB Small Business Optimism, JOLTS reports
- **Wednesday 3/12** – U.S. 25% tariffs on steel and aluminum imports to be deployed, CPI and Federal Budget Balances | Canada Bank of Canada rates decision and press conference
- **Thursday 3/13** – U.S. Initial jobless claims, PPI
- **Friday 3/14** – U.S. consumer sentiment, Congress must have budget passed or shutdown begins | Canada manufacturing and wholesale sales figures

Data scorecard as of March 5, 2025

Equity Market Total Returns						
	3/5/2025 Level	WTD	YTD	2024	2023	2022
S&P 500	5,843	-1.9%	-0.5%	25.0%	26.3%	-18.1%
NASDAQ	18,553	-1.6%	-3.8%	29.6%	44.7%	-32.5%
DOW	43,007	-1.9%	1.4%	15.0%	16.2%	-6.9%
Russell 2000	2,101	-2.9%	-5.6%	11.5%	16.9%	-20.5%
S&P/TSX	24,871	-2.0%	1.0%	21.7%	11.8%	-5.8%
MSCI EAFE	8,923	2.9%	10.4%	3.8%	18.2%	-14.5%
MSCI EM	597	1.7%	4.0%	7.5%	9.8%	-20.1%
Bond Market Total Returns						
		WTD	YTD	2024	2023	2022
Bloomberg U.S. Aggregate		-0.4%	2.3%	1.3%	5.5%	-13.0%
Bloomberg U.S. Treasury		-0.4%	2.3%	0.6%	4.1%	-12.5%
Bloomberg U.S. Corporate		-0.3%	2.3%	2.1%	8.5%	-15.8%
Bloomberg U.S. High Yield		-0.1%	2.0%	8.2%	13.4%	-11.2%
Bloomberg 1-10 Year Munis		0.0%	1.6%	0.9%	4.5%	-4.7%
Bloomberg Canada Aggregate		-0.4%	1.8%	4.0%	6.5%	-11.3%
Bloomberg Canada Treasury		-0.3%	2.0%	2.9%	5.0%	-9.9%
Bloomberg Canada Corporate		-0.3%	1.4%	6.9%	8.2%	-9.5%
Government Bond Yields						
	3/5/2025	Last Month End	Last Quarter End	2024	2023	2022
U.S. 10-Year Treasury	4.28%	4.21%	4.57%	4.57%	3.88%	3.88%
Canada 10-Year Government	2.97%	2.90%	3.23%	3.23%	3.11%	3.30%
U.K. 10-Year Gilt	4.68%	4.48%	4.56%	4.56%	3.53%	3.66%
German 10-Year Bund	2.79%	2.41%	2.36%	2.36%	2.02%	2.57%
Japan 10-Year Government	1.44%	1.37%	1.09%	1.09%	0.61%	0.41%
Currencies & Real Assets						
	3/5/2025 Level	WTD	YTD	2024	2023	2022
USD Index	104.28	-3.1%	-3.9%	7.1%	-2.1%	8.2%
CAD:USD	\$0.70	0.9%	0.3%	-7.9%	2.3%	-6.7%
Bitcoin	\$90,375.01	7.3%	-3.6%	120.5%	157.0%	-64.3%
Gold	\$2,919.39	2.2%	11.2%	27.2%	13.1%	-0.3%
Oil (WTI)	\$66.31	-4.9%	-7.5%	0.1%	-10.7%	6.7%

*Benchmark data does not reflect actual investment performance but reflects benchmark results of the underlying indices referenced.

Index Definitions

Equity indices

S&P 500® Index is an index of large-cap U.S. equities. The index includes 500 leading companies and covers approximately 80% of available market capitalization.

NASDAQ Composite Index is a market-cap weighted index of the more than 3,000 common equities listed on the Nasdaq stock exchange.

Dow Jones Industrial Average (“DOW”) is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and the Nasdaq.

Russell 2000® Index (Russell 2000®) is an unmanaged index that measures the performance of the smallest 2000 U.S. companies in the Russell 3000® Index.

S&P/TSX Index is a capitalization-weighted equity index that tracks the performance of the largest companies listed on Canada’s primary stock exchange, the Toronto Stock Exchange (TSX).

MSCI EAFE Index (Developed Markets —Europe, Australasia, and Far East Index) is a standard unmanaged foreign securities index representing major non-U.S. stock markets, as monitored by Morgan Stanley Capital International. The index captures large and mid-cap representation across 21 developed markets countries around the world, excluding the U.S. and Canada.

MSCI Emerging Markets Index is a market capitalization weighted index representative of the market structure of the emerging markets countries in Europe, Latin America, Africa, Middle East and Asia. Prior to January 1, 2002, the returns of the MSCI Emerging Markets Index were presented before application of withholding taxes.

Fixed income indices

Bloomberg U.S. Aggregate Bond Index is an unmanaged index that covers the U.S. investment-grade fixed-rate bond market, including government and credit securities, agency mortgage pass-through securities, asset-backed securities and commercial mortgage-based securities.

Bloomberg U.S. Treasury Index is an unmanaged index that includes a broad range of U.S. Treasury obligations and is considered representative of U.S. Treasury bond performance overall.

Bloomberg U.S. Corporate Bond Index measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD denominated securities publicly issued by U.S. and non-U.S. industrial, utility and financial issuers.

Bloomberg U.S. Corporate High Yield Index is an unmanaged index that covers the USD-denominated, non-investment-grade, fixed-rate, taxable corporate bond market. Securities are classified as high yield if the middle rating of Moody’s, Fitch and S&P is Ba1/BB+ or below.

Bloomberg 1-10 Year Blend Municipal Bond Index is a market value-weighted index which covers the short and intermediate components of the Bloomberg Capital Municipal Bond Index — an unmanaged, market value-weighted index which covers the U.S. investment-grade tax-exempt bond market.

Bloomberg Canada Aggregate Bond Index measures the investment grade, Canadian dollar-denominated, fixed-rate, taxable bond market. It includes treasuries, government-related, and corporate issuers.

Bloomberg Canada Aggregate Bond Index - Treasury is the treasury sub-component of the Bloomberg Canada Aggregate Bond Index, which measures the investment grade, Canadian dollar-denominated, fixed-rate, taxable bond market.

Bloomberg Canada Aggregate Bond Index - Corporate is the Corporate sub-component of the Bloomberg Canada Aggregate Bond Index, which measures the investment grade, Canadian dollar-denominated, fixed-rate, taxable bond market.



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