BC Investment Outlook

Spring 2025 Edition

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May 29, 2025 | 2:30 pm – 5:00 pm

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Navigating the Trump Era: Economic Realities and Investment Strategies

by ***John Nicola***
Chairman, Chief Executive Officer &
Chief Investment Officer

NICOLA WEALTH

John Nicola aims to objectively analyze what Trump is trying to accomplish with tariffs, the economic implications of his policies, and how they may impact markets.

As of when this was written, much has transpired:

- Equity markets have faced sharp volatility, with major indices like the Nasdaq, S&P 500, and TSX posting meaningful declines. These shifts have resulted in a considerable reduction in overall market value.
- In Canadian politics, following Justin Trudeau's resignation, the Liberals selected Mark Carney as their new leader, bringing a renewed focus on European trade and efforts to expand the Comprehensive CETA agreement. Canada continues to align more closely with Europe, particularly in its support for Ukraine. Carney's appointment marked a strategic shift for the Liberal Party as it positioned itself against Pierre Poilievre's Conservatives in the lead-up to the federal election.
- Meanwhile, trade tensions escalated when Premier Doug Ford announced a 25% tax on electricity exports to the U.S., prompting Trump to double duties on steel and aluminum to 50%. As of Tuesday, March 11, both sides have chosen to back down and, at least temporarily, reverse these decisions.
- The U.S. Federal Reserve now expects the country to enter a recession this year, possibly as soon as the first quarter. Meanwhile, Trump and Musk have unsettled not just the markets but also their own citizens, particularly in red states, through the impact of DOGE. While Republican leaders remain publicly silent on Trump, they have been vocal in private opposition. A full internal revolt, however, would likely require further market declines, rising unemployment, and increased inflation—all of which are possible.
- As of April 2, additional tariffs are being applied to multiple countries— including Canada—targeting sectors such as automotive and natural resources. In response, the Canadian government has signaled plans to introduce further tariffs on a broader range of U.S. imports, including a proposed levy on U.S. truck shipments transiting through British Columbia to Alaska. In short, both the rhetoric and the tariff measures are escalating, with no resolution currently in sight.

UNDERSTANDING TRUMP'S ECONOMIC APPROACH

What do I think Trump is trying to do? Let's examine what I think his belief systems are based on.

First, he really does think that tariffs are a great vehicle for raising taxes and are likely to accelerate the reshoring of manufacturing to the U.S. That in itself will lower the trade deficits that he believes damage the U.S. standard of living.

He also believes, as Reagan did, that lower taxes for the rich will result in the benefits of "trickle-down economics," eventually creating benefits for the bottom 50% of the income and wealth strata of U.S. society. He, along with Musk and his Silicon Valley mafia, believes that social safety nets are a major liability that will only get worse with time as the population ages.

It was Joseph Goebbels, Hitler's Minister of Public Enlightenment and Propaganda, who said, "Repeat a lie often enough and it becomes the truth." Trump's approach relies heavily on rhetoric and strong narratives to shape public perception and policy support.

This approach, however, is proving counterproductive on the global stage. Many countries—including those in Europe, Australia, New Zealand, and of course Canada—are not just imposing tariffs on U.S. products but are also experiencing consumer-led boycotts. If these boycotts prove successful, they could have a far greater impact on U.S. businesses than any tariffs will. To put it politely, Trump's policies have turned much of the world against the USA. He is stubborn enough to double down and inflict economic pain on his allies in particular. The long-term cost to the U.S. is incalculable. At some point, I hope and expect saner minds will prevail.

KEY ECONOMIC FACTS TO KNOW: A GLOBAL SNAPSHOT

What do I think Trump is trying to do? Let's examine what I think his belief systems are based on.

Let's add to this some interesting facts:

- **U.S. GDP** is projected to reach $30 trillion USD in 2025.
- The **U.S. budget deficit** is projected at $1.9 trillion USD for fiscal 2025, or about 6.3% of GDP.
- **Canada's GDP** in 2025 is projected to reach $3.1 trillion CAD. The projected deficit is just over $60 billion, or 2% of GDP for 2024-25, depending on the fiscal policies our next government implements. In addition, there are provincial deficits and debts, which, when combined, total approximately $2.2 trillion CAD on a net basis, or about 75% of GDP.
- The **U.S. federal debt-to-GDP** ratio (not including state or municipal debt) is 124% and has risen to that level from less than 40% in 1970 *(Figure 1)*.
- **China is not in a better fiscal position than the U.S.** The country's total debt burden, including individual and corporate debt, reached 310% of GDP in 2024, one of the highest in the world.
- The **U.S. Social Security Fund** holds nearly $3 trillion USD in assets, all invested in U.S. bonds, which earn an average return of around 4%.

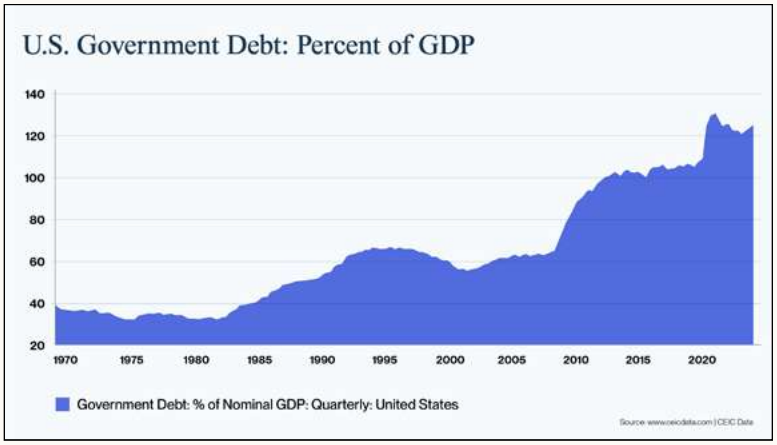


Figure 1

- The **Canada Pension Plan (CPP)** has assets of almost $700 billion CAD in an economy that is roughly 1/15th the size of the U.S. The CPP has delivered a 10-year annualized return of 9.2%.

If Canada does enter a recession this year, the government and the Bank of Canada have a range of fiscal and monetary tools at their disposal. Canada's deficit-to-GDP ratio is smaller than that of the U.S., and our combined provincial and federal debt-to-GDP ratio is also notably lower. The Bank of Canada could accelerate interest rate cuts, which would likely weaken the Canadian dollar and help offset some of the impact of U.S. tariffs.

THE IMPACT OF TARIFFS: WINNERS, LOSERS, AND MARKET REPERCUSSIONS

The U.S. does run large trade deficits with China, Europe, Mexico, and Canada, though much of Canada's surplus is driven by energy exports. However, the U.S. also has a $250 billion trade surplus in services, which does not account for revenue generated by U.S. firms' subsidiaries abroad. An interesting question is how other nations might respond to counterbalance that surplus in retaliation for tariffs on goods. For example, Premier Doug Ford recently took such action by cancelling a $100 million contract with Starlink.

Currently, the weighted average of Canadian tariffs is about 1.4% on all imports, yet we impose almost 7% on interprovincial trade in goods. When services are added, that amount might exceed 20%, depending on the specifics. This presents a remarkable opportunity: eliminating these internal barriers could boost our GDP by 3-8%. This potential growth stands in stark contrast to forecasts suggesting Trump's new tariffs could reduce Canada's GDP growth to 0% this year and -2% next year. The implications are clear: **we have a powerful economic offset to external tariffs entirely within our control**.

Below, I have included a slide from a recent presentation showing a graph with expected revenues from U.S. tariffs *(Figure 2)*. However, the graph assumes buying habits won't change with tariffs. The final numbers will likely be far lower. The second chart illustrates who in the U.S. will bear the burden of these tariffs, and it is overwhelmingly the poor *(Figure 3)*.

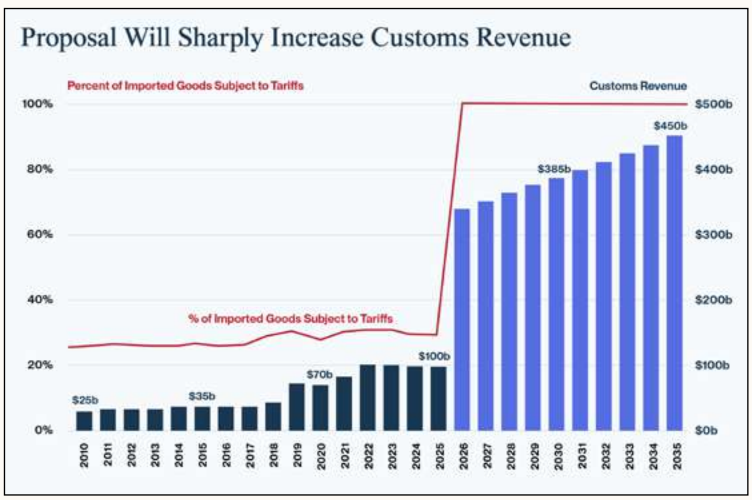


Figure 2

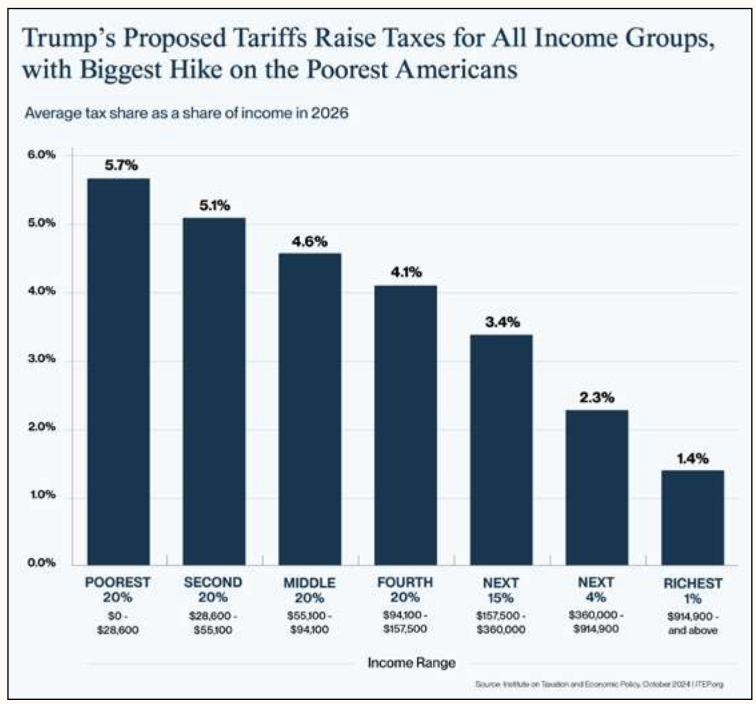


Figure 3

To avoid the impact of tariffs, some wealthy Canadians have suggested moving their businesses—and even themselves—to the U.S. While this is not a detailed analysis of the situation, consider this: the U.S. federal tax rate on C Corps is 21%, with most states adding taxes as high as 9.8%. In Canada, larger corporations face a combined federal and provincial tax rate of 27%, while small businesses benefit from a 11-12% tax rate (an advantage not available in the U.S.). Many Canadians also overlook the exit tax when changing residency, which could easily amount to 20-25% of an individual's net worth. Those with significant wealth who relocate to the U.S. will also eventually be subject to U.S. estate taxes of up to 40% on their worldwide assets.

All of this brings to mind a line from a Laurel and Hardy movie: "Well, here's another nice mess you've gotten me into."

A HISTORICAL PERSPECTIVE ON ECONOMIC RESILIENCE

So, what can we do with this mess, and how will it impact markets and the economy?

History provides perspective. Over the last 111 years, we have endured two World Wars, a Great Depression, a Cold War that lasted 45 years, 20% interest rates of the early '80s, the Dot-Com Bubble, the Great Financial Crisis, the first Trump presidency, and multiple health crises. Despite it all, we emerged far wealthier and healthier on both a local and global scale than we were at the start. We'll survive this too.

That, however, does not mean we should not be proactive in our planning and investment strategies.

INVESTMENT STRATEGY: PREPARING FOR VOLATILITY

These are some of the outcomes we are preparing for:

Public Equities: Focus on Stability

Expect volatility; focus on value stocks and dividend-paying companies.

- U.S. equities were already overvalued when Trump was elected.
- Tariffs will likely weigh on corporate earnings, making it unlikely that we will see the euphoric returns of the past two years. It is time to play defense.
- One of our key areas of research is dividends and their durability within our Canadian equity strategies. For example, a portfolio of 25 large-cap Canadian stocks with strong dividends has a weighted yield of approximately 5.5%, which, in a taxable Canadian account, is equivalent to an 8% yield on bonds. This market is likely to favour value investors and stock pickers.
- I asked our analysts to compare the volatility of these companies' dividends to the volatility of their stock prices, and the dividends proved to be five times less volatile. This strategy is centered on investing in sustainable cash flow. A focus on dividend investing will help strengthen our defensive position, and we plan to develop a high cash flow dividend strategy in short order.

Fixed Income: Balance Risks

Balance inflation concerns with recession risks; consider defensive allocations.

- Fixed income is trickier to rationalize because tariffs tend to be inflationary, which could force central banks to raise rates. However, tariffs are also likely to decelerate growth, increase unemployment, and could possibly trigger recessions in Canada, the U.S., and Europe (China would follow closely). In that case, we could see flat or lower rates and an economy experiencing stagflation.

- Personally, I lean toward the possible recession camp and do not see much room for rates to move higher. Over the last two years, we have strategically adjusted our allocations to fixed income, which proved to be a strong move. My inclination is to stay the course with fixed income, and for those looking to be more defensive, consider increasing that allocation.
- We are looking at introducing a credit hedge fund and are currently awaiting tax advisor input before proceeding.

Private Equity: A Long-Term Play

Long-term growth potential as public markets shrink.

- I am more optimistic about the prospects for private equity returns over the next decade than public equity returns. One key reason is that private equity as a percentage of global wealth is increasing as more companies choose not to be publicly traded and remain privately held *(Figure 4)*. Over the past 30 years, the number of public companies in the U.S. and Canada has decreased by 40-50%.

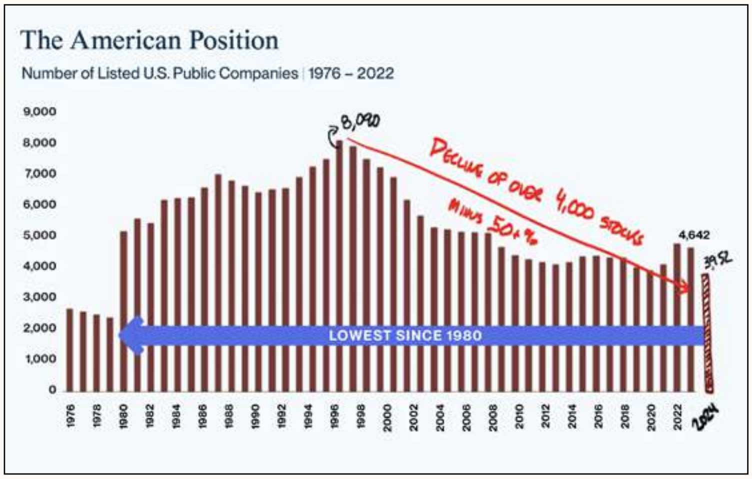


Figure 4

Real Estate: Selectivity is Key

Focus on high-demand sectors like multifamily, industrial, and specialty assets.

- This brings us to real estate (excluding housing). The past two years have been challenging for many investment-grade real estate portfolios, with a number of funds closing or gating. While we didn't experience that, our returns for our real estate limited partnerships for 2023 and 2024 were generally lower than our historic results, which have typically ranged from 9-13% annually over the last decade. Interest rates have started to turn the corner (more so in Canada than the U.S.), and that is beginning to impact cap rates for high-quality assets. Tariffs will not help the economic environment, which I would expect to weigh on real estate returns on a net basis.
- Our strategy remains to avoid office and retail assets, focusing instead on multi-family residential, specialty assets (such as self-storage and senior facilities), and industrial properties. Currently, our occupancy rates are relatively high and stable, so cash flows remain strong. This will continue to be the focus for our income funds.
- The Nicola Value Add Real Estate Limited Partnership, a fund of about $1 billion, has $170 million in cash to deploy, with another $300 million in cash expected in 2025. This is a buyer's market for development assets, and we are well-positioned with the cash to invest.

INVESTMENT STRATEGY: PREPARING FOR VOLATILITY

We are now fully in the Trump era and should prepare for trying times. Canada has already begun implementing policies to mitigate some of the damage by seeking new export markets and breaking down interprovincial trade barriers. However, these efforts will not completely offset the worst effects of tariffs, and given Trump's unpredictable behaviour, we cannot anticipate what further actions he may take (such as intimidating Canada into joining as the '51st State').

If I were to outline my vision for Canada's economic trajectory over the next 3–5 years, it would include the following:

- Reducing trade dependency on the U.S. to below 50%, particularly in materials and services that are difficult for them to replicate (e.g., energy and potash).
- Expanding CETA as much as possible with Europe and developing a trans-Pacific trade model to double our trade with that region.
- Eliminating 90% of interprovincial trade barriers.
- Refining immigration policy to attract top global talent, including from the U.S.
- Properly funding our military commitments, as we have in the past when necessary.
- Developing a robust industrial policy focused on R&D and productivity.

That said, as I wrote above, **Trump will eventually pass from the political stage**, and his policies will not endure if they fail to improve American prosperity—which I strongly suspect they will not. Some efforts to reduce government bureaucracy and waste make sense in principle, though not in the way Elon Musk is attempting to achieve that goal.

Charles Darwin's seminal work, On the Origin of Species, explained the concept of survival of the fittest as "the natural process by which organisms best adjusted to their environment are most successful in surviving and reproducing."

We are now in a new environment—one in which we must not only survive but also adapt and position ourselves to thrive through diligence and the right tools. While market conditions continue to shift rapidly, **our core philosophy on portfolio design and management remains unchanged,** offering stability amid uncertainty.

John Nicola CFP®, CLU®, CHFC
Chairman, Chief Executive Officer & Chief Investment Officer, Nicola Wealth

A veteran of the financial services industry since 1974, John provides strategic leadership to Nicola Wealth, exercising his passion for providing innovative solutions to clients' complex problems.

His areas of expertise include investment management, estate and financial planning, as well as business planning with a focus on best practices for wealth building, exit strategies, and shareholder agreements.

In 2011, John was named the Ernst & Young Entrepreneur of the Year (Financial and Professional Services, Pacific Region). In 2015, he was named B.C. CEO of the Year (Small-Medium Private Company) by Business In Vancouver. In 2016, he was recognized as one of Canada's Most Admired CEOs. Recently, he won the Ernst & Young Entrepreneur of the Year (Pacific Region) and was one of the ten National Winners of the Ernst & Young Entrepreneur Of The Year 2022 National Award. In 2023, he received the Lifetime Achievement Award from Wealth Professional. In 2025, John was inducted into the Business Laureates of BC Hall of Fame., recognizing his decades-long contributions to business and philanthropy. He was also named to Vancouver Magazine's 2025 Power 50 List alongside David Sung, highlighting their shared commitment to giving back.

John currently serves as Chair of the Nicola Wealth Board of Directors. Additionally, he is a Founding Member of CALU (Conference for Life Underwriters) and has continued to contribute to the organization for example, by serving as Chair for the 2003 annual meeting.

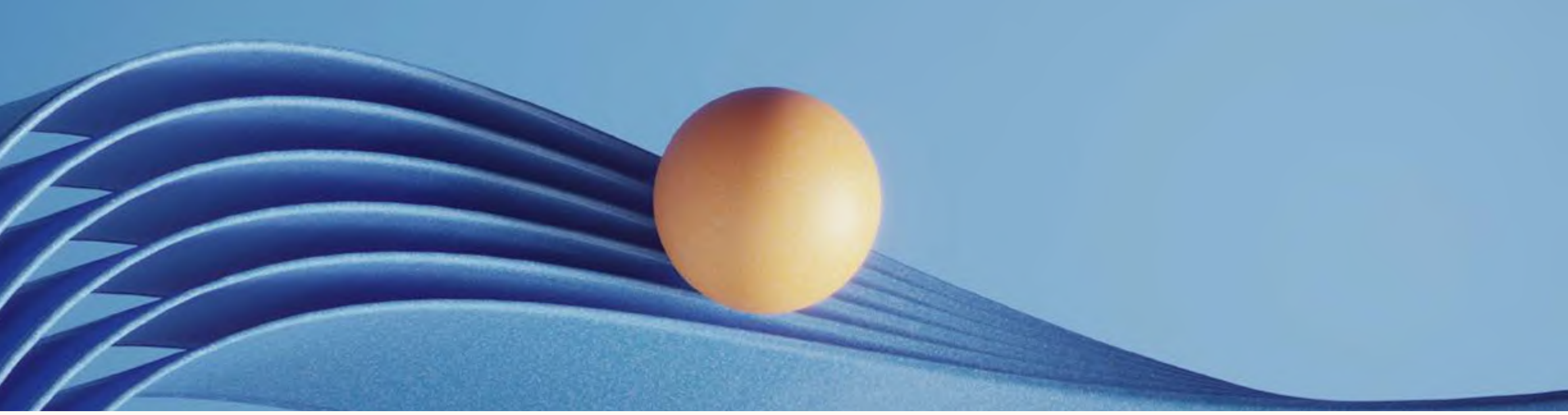
John has used his business acumen to help develop and grow several not-for-profit organizations over a number of years. These include Covenant House, an organization providing safe housing and holistic care to at-risk youth ages 12-24, The Pivot Law Society, a volunteer legal society defending the underrepresented issues facing Vancouver's Downtown Eastside, and Bulembu International, a foundation dedicated to helping an abandoned African mining village become self-sufficient.

Seeking Stability

*by **Tiffany Wilding**,*
Managing Director and Economist at PIMCO and
***Andrew Ball**s, Chief Investment Officer for*
Global Fixed Income at PIMCO

PIMCO

At a time of sweeping geopolitical change and clear challenges for riskier assets, bond markets offer a source of stability.



KEY TAKEAWAYS

The world has entered a period of geopolitical uncertainty, with the U.S. now at the center of the storm. Here are our near-term economic views:

- **Global uncertainty**: The Trump administration has taken aggressive early measures to address trade deficits and shrink the size of government. It remains unclear whether the current policy volatility will evolve into a more stable U.S. strategy. As tariff barriers rise, global uncertainty is increasing, particularly for export-dependent economies.
- **Threats to U.S. exceptionalism**: With both business and consumer confidence declining, the U.S. economic and financial-market exceptionalism of recent years could be fading.
- **National interests take new precedence**: Protectionist U.S. policies, coupled with the prospect for government spending cuts, are stoking concerns about U.S. recession risks and a rekindling of inflation. In contrast, the prospect of increased fiscal spending is improving the outlooks for countries such as Germany and China. Major central banks will aim to continue easing policy to neutral levels.

This newfound U.S.-led uncertainty has fueled a sell-off in risk assets and a surge in volatility. Meanwhile, high quality bonds have flourished, delivering comparable total returns to equities over the past year while offering favorable valuations today. Here are our near-term investment views:

- **Seek stable sources of return in turbulent times**: Historically, starting bond yields closely correlate with five-year forward returns. Yields are attractive today, positioning bonds well in this environment. We believe it's a good time to reduce concentrated positions in U.S. risk assets, particularly with valuations still elevated.
- **Diversify across global markets**: Global fixed income opportunities remain robust, offering strategies to further enhance diversification.
- **Favor asset-based finance over corporate credit**: We prefer asset-based finance relative to corporate credit across public and private markets.

ECONOMIC OUTLOOK: GLOBAL REORDERING

Pandemic disruptions are behind us. Labor markets have normalized. Although inflation in developed market (DM) economies may linger above post-financial-crisis averages, it's broadly within reach of central bank targets. Monetary policy is gradually returning to more neutral levels.

The focus has turned to a new disruptor: U.S. policy. The Trump administration, elected on a platform of change, is pledging to pursue three interconnected goals that will reshape the U.S. and global economies:

1. Balancing the U.S. trade deficit *(see Figure 1)*
2. Reducing elevated fiscal deficits
3. Reversing the decades-long decline in the U.S. labor force's share of income

Correcting these imbalances would require structural changes, including curbing the share of GDP derived from consumption in the U.S., reducing the contribution to GDP from manufacturing and savings in trade surplus economies, and lowering the concentration of global excess savings flows entering U.S. capital markets.

Implementing these changes faces economic, political, and market constraints, both in the U.S. and abroad. Doing so over a six- to 12-month cyclical horizon would likely disrupt economies and markets, even if the result is eventually a more balanced global system.

We anticipated such disruption in our January 2025 *Cyclical Outlook*, "Uncertainty Is Certain." Policy uncertainty is now unfolding daily and emanating mainly from the U.S., historically a source of global stability.

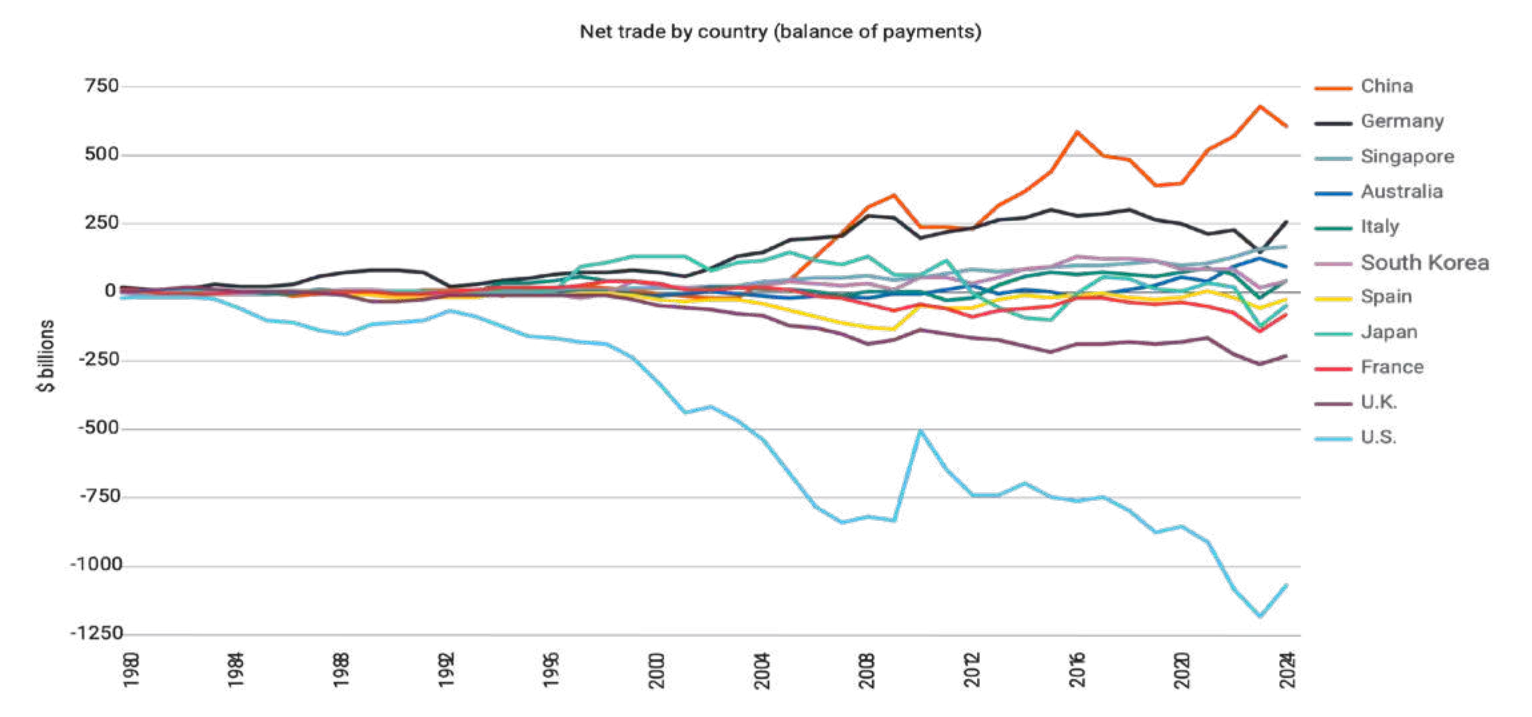


Figure 1

Source: World Bank, Haver Analytics, and PIMCO as of December 2024

THREATS TO U.S. EXCEPTIONALISM

This shift reflects an international role reversal, with the U.S. signaling a pullback from some traditional functions while other countries step in to fill the voids. Long-held assumptions about the U.S. as a reliable international leader are being challenged.

These changes may coincide with the twilight of the recent U.S. capital markets' outperformance relative to the rest of the world. In Europe, the peace dividend – the economic benefits of reduced military spending after the end of the Cold War – looks to be over, with countries across the continent now set to increase their defense budgets.

In January, we said our baseline called for an economically manageable increase in tariffs – which, along with U.S. tax and spending policy, would leave federal fiscal deficits largely unchanged in 2025 and 2026.

However, we also said these pivots, depending on their scope, widened the range of possible growth outcomes in the U.S. and deepened economic risks elsewhere, especially for countries heavily reliant on global trade and that run surpluses with the U.S. We thought U.S. equity market volatility would be a limiting factor.

The Trump administration has since launched aggressive measures on trade, government containment, and immigration. These are likely to slow the U.S. economy more than previously expected and hurt the labor market, regardless of whether government spending cuts are codified into law.

Officials have argued that some near-term pain is acceptable in pursuit of longer-term goals, suggesting the tolerance for economic and market volatility is higher than previously thought. Eventually, higher prices, especially for food and energy, and lower equity values are likely to be a political constraint.

RISING RISKS TO U.S. GROWTH AND INFLATION...

While the ultimate implementation remains uncertain, disruptive U.S. policy announcements have already damped U.S. consumer and business sentiment and will likely weigh on investment and hiring decisions *(see Figure 2)*. Globally, if businesses face tariff-related risks that are close to impossible to calibrate, then the likely result is delayed decisions on investment and expansion. In other words, tariff uncertainty is proving to be a headwind to growth, even if tariffs fail to materialize.

We see a risk that U.S. growth and labor market momentum downshift more decisively. After U.S. real GDP grew 2.5% to 3% annually over the past few years, we expect a below-trend pace in 2025 and 2026.

The average effective tariff rate on U.S. imports has increased an estimated 7.5 percentage points from actions against Canada, Mexico, and China. We expect additional trade policy measures to raise that figure significantly throughout the year, as Europe and other southeast Asian countries could face U.S. tariffs.

U.S. sentiment surveys have deteriorated

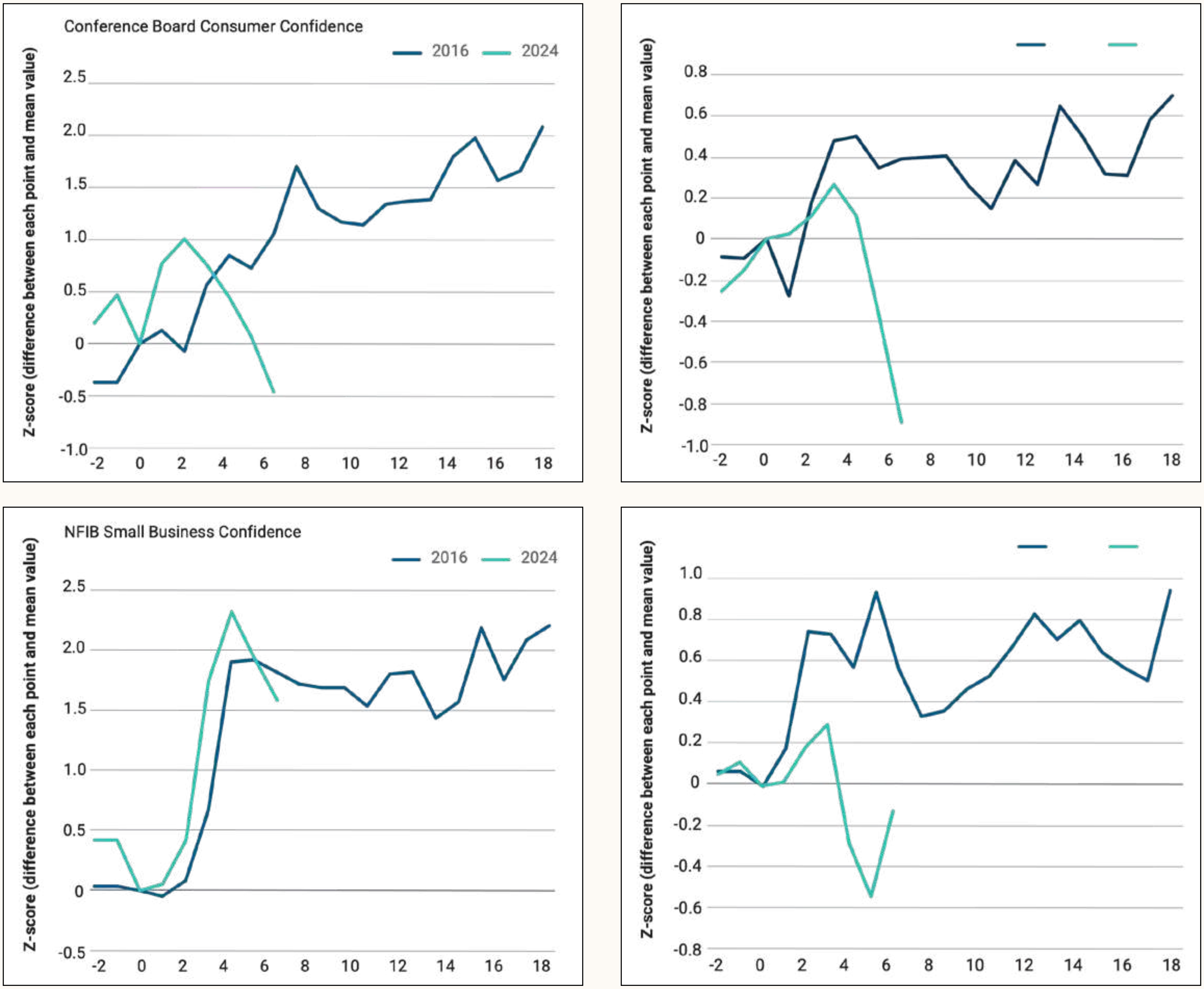


Figure 2

Source: Conference Board, University of Michigan, S&P, NFIB, Haver Analytics, and PIMCO as of March 2025

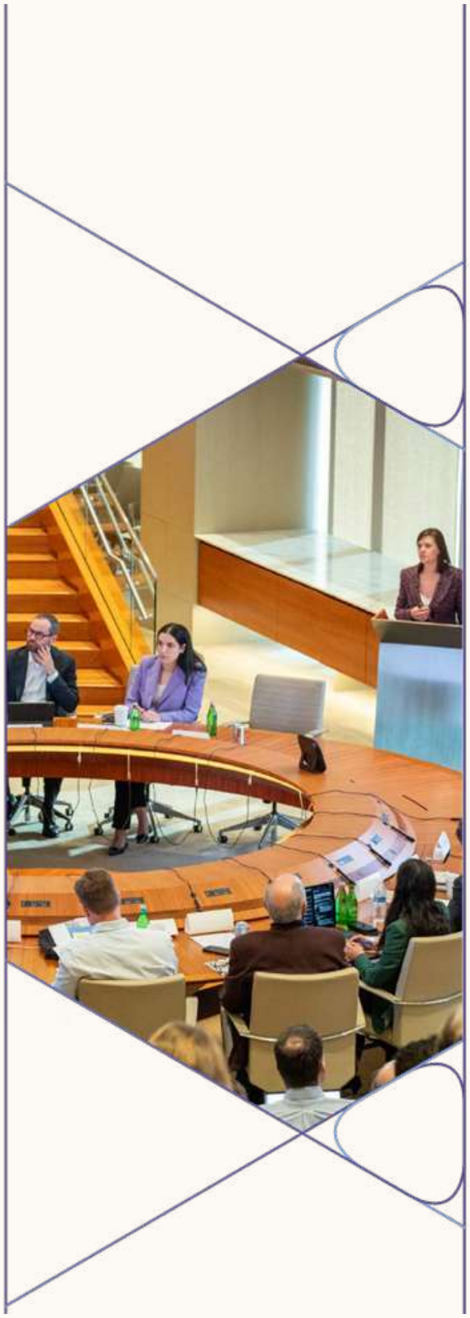
Businesses are likely to pass on tariff costs, boosting inflation during the period of price adjustment and delaying the return to the Federal Reserve's 2% target. More concerning for Fed officials, surveys of consumers and business suggest inflation expectations are moving higher.

In Congress, the focus is already on U.S. tax policy. Given the circuitous nature of the legislative process and the very narrow Republican majorities, especially in the House of Representatives, we do not expect to see a signed bill until summer, if not later. While we still expect trade, spending, and tax policies to have a neutral net effect on the U.S. fiscal impulse in 2025, a more significant near-term growth slowdown could tilt the scales toward larger, more stimulative tax cuts.

… WHILE POTENTIAL FOR FISCAL STIMULUS AND RATE CUTS HELPS THE GLOBAL OUTLOOK

Recent policy actions in other major economies appear to incrementally improve what were otherwise bleaker outlooks. Expectations for fiscal expansion are rising in countries such as China, Germany, Japan, and Canada.

China and Germany have strong incentives to implement structural changes. China's housing overbuild and debtdeflation cycle contributed to an overreliance on exports – a model now strained by other countries' unwillingness to import China's production capacity. China appears more willing to implement policies to boost consumption while continuing to invest in technology and AI.



Germany is prioritizing increased spending on defense and infrastructure after the pandemic, the war in Ukraine, and intense competition from China have upended the German economic model. Other European countries could follow suit but may have less capacity than Germany, which tends to run fiscal surpluses.

We expect growth trends to remain stable and mediocre outside of the U.S. Trade uncertainty remains a headwind, but easier financial conditions in more interest-rate-sensitive economies and fiscal loosening should provide some offsetting support.

Looser labor markets and an expected moderation in wage inflation should keep inflation outside of the U.S. on a declining path, allowing DM central banks to continue easing policy to neutral levels. We expect 50–100 basis points (bps) of additional rate cuts across DM economies over the rest of 2025. The Bank of Japan remains an outlier and is likely to raise rates in the face of elevated inflation expectations.

As a baseline, we expect the Fed to cut rates by another 50 bps later this year. The Fed is in a tricky spot, as higher inflation and lower growth risks have contrasting implications for the central bank's price stability and full employment goals.

The main risk is that slowdowns in the labor market and real GDP growth cause the Fed to cut rates more deeply than the market is currently pricing, even if sticky inflation and rising inflation expectations delay the Fed's reaction to early signs of an economic downturn. In the end, we expect Fed officials will cut more aggressively if they see recession risks rising faster than inflation expectations. In contrast, we believe the likelihood of the Fed reversing course and hiking rates in response to tariff-related inflation is low.

INVESTMENT IMPLICATIONS: SEEK SIMPLICITY, STABILITY, AND DIVERSIFICATION

In this unusually uncertain macroeconomic environment, it's prudent to prioritize simple, stable investments over trying to predict the unpredictable.

Elevated uncertainty is likely to challenge the U.S. equity outperformance of recent years. There is a strong case to diversify away from highly priced U.S. equities into a broader mix of global, high quality bonds. We believe we are in the early stages of a multiyear period in which fixed income can outperform equities while offering a more favorable riskadjusted profile.

Historically, starting bond yields correlate very closely with five-year forward returns *(see Figure 3)*. Yields on high quality bond portfolios are 4.65% based on the Bloomberg US Aggregate Index, and 4.80% based on the Global Aggregate Index (U.S. dollar hedged), as of 28 March 2025. Building on that baseline, active managers can identify opportunities in high quality sectors to seek alpha – returns above market benchmarks – to enhance the yields investors earn.

Meanwhile, the equity risk premium – a measure of the additional returns investors require to invest in riskier equities – turned negative in late 2024 for the first time in more than two decades, driven by historically elevated stock valuations coupled with the highest bond yields in years. It has since risen but remains near historical lows. (For more, see our February PIMCO Perspectives, "Where to Look When Equities Are Priced for Exceptionalism."

The portfolio diversification benefits of bonds have been on display in recent months. Equities and bonds typically move in opposite directions, allowing one part of a balanced portfolio to gain when another falters. As stocks have slumped, high quality bonds have thrived, delivering total returns comparable to equities over the past year while presenting favorable valuations today.

DURATION LOOKS MORE ATTRACTIVE

It remains unclear whether recent market volatility marks peak pessimism regarding U.S. policy uncertainty, or if the disruption will persist and further erode business and consumer confidence both in the U.S. and abroad, affecting economies and asset prices even more.

The rosy assumptions that buoyed risk asset pricing earlier this year have given way to a more cautious outlook. The decline in risk assets has accompanied a rally in U.S. Treasuries and Canadian government bonds, which contrasts with higher yields in Europe and the U.K. – in part the result of Germany's planned fiscal spending increase.

Even after this year's Treasury rally, the U.S. 10-year note yield remains firmly in the middle of our expected cyclical range of 3.75%–4.75%. However, if recession risks rise, there is the potential for markets to price in more Fed rate cutting and for this range to shift down.

The German bond market experienced a sharp repricing in early March, reflecting changing political attitudes toward public spending. This shift is significant, given Germany's unique position in the eurozone with its low debt levels.

Strong link between starting bond yields and 5-year forward returns

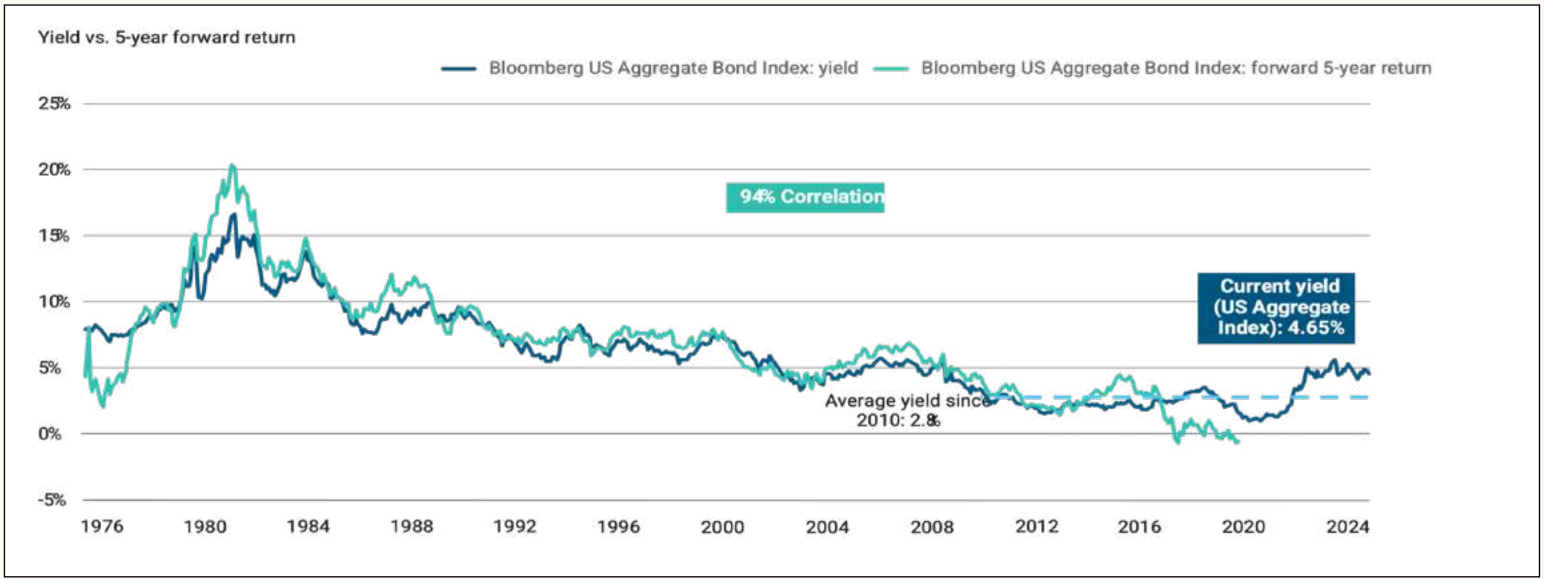


Figure 3 Source: Bloomberg, PIMCO as of 28 March 2025. **Past performance is not a guarantee or a reliable indicator of future performance.** Chart is provided for illustrative purposes only and is not indicative of the past or future performance of any PIMCO product. Yield and return are for the Bloomberg US Aggregate Bond Index. It is not possible to invest directly in an unmanaged index.

Beyond Germany, we expect increased defense spending across Europe – though with measures likely to be less bold, given that countries with weaker initial fiscal conditions will struggle to fund such initiatives. Consequently, we have raised our expected range for the 10-year bund yield to 2.5%–3.5% from 2%–3%, indicating potential for further repricing.

Broadly, we favor an overweight to duration, a gauge of interest rate sensitivity. At a time of asymmetric risks across countries, we look to global diversification in high quality duration. We favor the U.K. and Australia for overweight duration positions. We view European duration as less attractive, given fiscal pressures, and expect yield curves to steepen across eurozone markets.

RICH GLOBAL OPPORTUNITIES

The flip side of serial U.S. trade deficits has been the glut of foreign excess savings fueling U.S. capital markets. The world has been heavily weighted toward U.S. investments, particularly equities *(see Figure 4)*, which now appear more vulnerable.

In this environment, we believe it makes sense to capitalize on global opportunities, particularly as bonds have become more attractive. In high quality duration, in credit, and in securities markets, we will look to emphasize the global opportunity set.

Emerging markets (EM) offer interesting alpha opportunities as well as diversification benefits. In high quality EM, historical default rates align with U.S. corporate credit, and premiums for structuring and illiquidity remain attractive. We see value in local currency opportunities that could benefit from capital flows being redirected from the U.S., as well as in hard dollar spreads where investment grade credit is increasingly available.

U.S. now constitutes more than 70% of the MSCI World Index

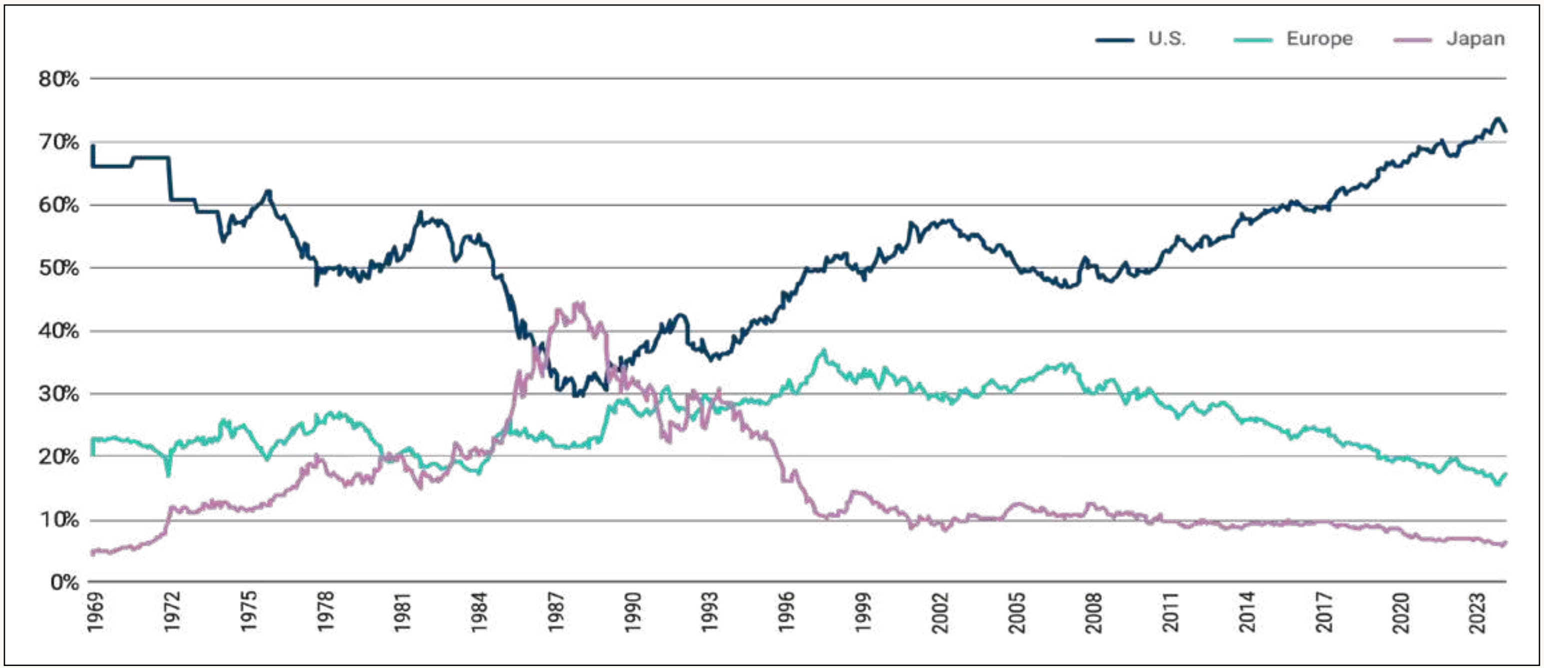


Figure 4

Source: Datastream, PIMCO calculations as of 27 March 2025

The risks to U.S. exceptionalism have reduced the attractiveness of the U.S. dollar. At the same time, tariff risks caution against short positions in the U.S. dollar, in case currency adjustment is the release valve should unexpected tariffs cause other currencies to depreciate. We favor carefully managed foreign exchange positions, to generate income outside of the U.S. while seeking to minimize correlations to the U.S. dollar or equity markets.

FAVOR ASSET-BASED FINANCE OVER CORPORATE CREDIT

We are cautious on corporate credit, as we believe spreads fail to adequately account for potential downside risks.

While corporate bonds play an important role in portfolios, we currently see greater value in high quality alternatives. That includes credit derivative indices and an overweight position in agency mortgage-backed securities (MBS). We prefer high quality fixed income and securitized products.

In private credit, we believe asset-based finance (ABF) strategies offer the most favorable opportunities and entry points. We can identify attractive cash flow profiles that are typically fixed-rate, amortizing, and secured by tangible assets. This creates a narrower range of outcomes, making ABF a valuable addition to portfolios as other private credit assets face increased uncertainty.

This is especially true in corporate direct lending, where demand/supply imbalances (with more investor demand for loans than borrowers seeking solutions), weaker lender protections, and floating-rate coupons lead to a wider range of outcomes. We see competition in this space increasing, with significant investor dry powder chasing deals and banks returning to syndicated loan markets.

This is contributing to convergence in spreads between public and private leveraged credit markets. Contrary to expectations that the Trump administration would ignite merger and acquisition activity, heightened uncertainty has hindered M&A and slowed new deal flow.

CONCLUSION

With stock valuations and volatility unusually elevated, and credit spreads tight, high quality fixed income can offer attractive yields, stability, and a robust longer-term outlook for patient investors.

Tiffany Wilding
Managing Director and Economist at PIMCO

Tiffany Wilding leads PIMCO's Cyclical Forum, shaping the firm's global economic outlook and analyzing key macroeconomic risks for the Investment Committee. She also co-chairs the Americas Portfolio Committee.

Andrew Balls
Chief Investment Officer for Global Fixed Income at PIMCO

Andrew Balls oversees PIMCO's global fixed income strategies, managing portfolios and leading investment teams across Europe, Asia-Pacific, and emerging markets. He is a member of the firm's Investment Committee.

Deglobalisation's Impact on Infrastructure

by ***Jacob Otto,***
Director, Head of Product Specialists – EMEA

IFM Investors

Deglobalisation is emerging as a major driver of infrastructure debt opportunities, as the US and Europe look to onshore vital industries.

Deglobalisation's Impact on Infrastructure

KEY TAKEAWAYS

1	We believe a renewed focus on the reshoring of industries and building economic self-sufficiency will present investment opportunities.
2	Energy policies and the power generation and transportation landscape are evolving differently in the US and Europe.
3	Protecting growth drivers such as the digital economy and advanced manufacturing will require increased infrastructure investment, from fibre networks, data centres, factories and logistics to transportation.

In many ways, the global economy is more deeply interconnected today than at any point in human history. However, deglobalisation has become a popular political talking point, spilling into investor discussions. While we believe the global economy will remain fundamentally interconnected for years to come, we also believe there will be a renewed focus on reshoring of industries and building national economic self-sufficiency, ultimately impacting the patterns of global trade. These trends are driven by, among other things:

- Heightened geopolitical tensions
- Economic nationalism spurred by global competition, the heightened cost of living, immigration concerns, and offshoring
- Supply chain vulnerabilities
- Changes in the resource mix needed to power economic growth and resilience

These movements will shape the next wave of infrastructure investment. Politics and infrastructure have always been heavily intertwined. Support for infrastructure can take many forms and is particularly important for greenfield infrastructure development and growth. A wave of deglobalisation will particularly impact infrastructure investment through:

1) The promotion of energy independence, and

2) Protecting future drivers of growth domestically

These policies will help shape our outlook for debt investing in infrastructure sectors over the coming quarters. In this paper we will consider the landscape in both Europe and the US.

PROMOTION OF ENERGY INDEPENDENCE

Each nation's pursuit of energy independence will look different based on its available natural resources and attitudes towards reducing emissions.

EUROPEAN PERSPECTIVE

In Europe, globalisation led to a reliance on cheap, imported Russian gas, the risks of which became obvious with the outbreak of the

Russia-Ukraine war. Immediate actions included increasing imports of hydrocarbons like Liquefied Natural Gas (LNG) from friendlier countries, with the US becoming the leading LNG exporter in 2023. Given Europe's political support for decarbonisation, domestic energy production increases will focus primarily on renewables, where solar, wind, and hydroelectric power have all played a role. Europe has consistently installed around 15 GW of wind capacity over the past 10 years[1], of which around 80% has been onshore. We expect to see further growth in the offshore sector, although supply chain and performance issues could slow deployment. Solar power continues to be very cost-competitive; however, reliable sunshine and land-use trade-offs challenge widespread deployment.

Countries will also need to find ways to generate and transport low-carbon power from places where it is efficient to create, to where it needs to be consumed. Not every country can feasibly deploy commercially viable renewables capacity to power their own grids.

Policy initiatives such as the European Green Deal and the REPowerEU plan have supported the renewables rollout. Norway and Sweden are now two of the largest power exporters to continental Europe via their surplus hydroelectric power. However, in our view, relying on trading energy with regional allies will not be sufficient to meet increasing electricity demand and energy security goals. More capacity is needed, and here Europe will need a multi-faceted approach.

This presents key opportunities for infrastructure debt investors, such as:

- **Increased wind and solar development**: We anticipate continued wind and solar growth, with solar expansion mainly in southern Europe, alongside the UK potentially sourcing renewables via undersea cables from Morocco[2].
- **Grid upgrades**: Europe will need to modernise and interconnect power grids across countries to truly benefit from more renewable energy generation. Investment opportunities lie in domestic grid infrastructure, interconnectors, other transmission infrastructure, and direct feedlines from energy generation sources for energy-intensive projects in the nascent hydrogen economy or for high-powered data centres.
- **Other renewable sources**: Biomass and biogas are 24/7 sources of renewable power that can help balance electricity grids. The key is to ensure sustainable and reliable feedstock sources. Geothermal and potentially increased hydroelectric power in places like the Pyrenees and Alps may also have a role to play.
- **Power generation with carbon capture, utilisation, and storage (CCUS)**: Power assets across Europe are responding to evolving climate policy by accelerating efforts to deploy CCUS at commercial scale, with energy from waste and biomass plants driving deployment.
- **The role of nuclear**: The politics of nuclear generation in Europe is complicated. Germany, which produced as much as 170 TWh/year of nuclear power in the 1990s, shut down its last nuclear plant in 2023[3]. Many other reactors in Europe are nearing the end of their useful lives. If these are shut down, even greater investment will be needed in renewables. However, shifting political tides may plant the seeds of a nuclear renaissance akin to what is being seen in the US, which may include small modular nuclear reactors.

[1] Wind energy in Europe: 2023 Statistics and the outlook for 2024-2030, WindEurope
[2] Xlinks Morocco-UK Power Project
[3] Q&A - Germany's nuclear exit: One year after, Clean Energy Wire

CASE STUDY

WASTE-TO-ENERGY PLANT[4]

Funds advised by IFM Investors provided debt financing for the second largest waste-to-energy operator in the Netherlands. The business is focused on the processing and incineration of municipal, commercial and hazardous waste to generate energy, leading to a reduction in waste volumes going to landfill. It earns revenues through the collection of waste (gate fees) and the sale of energy.

The company has two facilities with a combined permitted capacity of 1,700 kt/year. The first is strategically located next to the Port of Rotterdam, and the second is on the outskirts of the City of Arnhem, near Germany. We believe both locations are well positioned to receive and process waste and supply energy to continental Europe. The business has plans to build and operate a large CCUS facility in the medium term. Currently, this business is the only waste-to-energy operator with a commercial CCUS facility, and its port location will enable it to leverage existing infrastructure to deploy undersea carbon storage. IFM believes the growth plans combined with its strategic locations mean the business is competitively well positioned to gain market share.

[4] Case studies are provided for illustrative purposes only and should not be relied on to make an investment decision.

US PERSPECTIVE

In the US, political tides have shifted to prioritise energy independence and export, with climate goals taking a back seat. The US possesses an abundance of energy resources, and the Trump administration seems focused on leveraging these resources to maintain energy independence.

After years of relatively flat power demand, two key trends are pushing demand forecasts upward. Electrification of heating and transportation will strain power grids, moving peak demand from summer cooling into winter heating and increasing daily swings tied to electric vehicle (EV) charging. Increased domestic industrial output through an emphasis on onshoring and digitisation of the economy are now being supercharged through billions of dollars of investment in generative AI technologies – representing an opportunity to invest in data centres and the infrastructure to power them. Within the power market, other key investable themes include:

- **Natural gas as a transition fuel**: Natural gas remains a highly efficient source of reliable baseload power and will continue to push out older, inefficient technology and coal fired power. Gas power plants can also step in quickly to maintain grid reliability against fluctuating renewable power output.
- **Solar and wind projects continue**: Even with potential political headwinds, solar and wind capacity can expand in the US, to the extent that projects remain economically competitive. Many projects remain supported at the state level. Broadly speaking, institutional investors may replace funding from the Inflation Reduction Act for economically viable projects. Offshore wind development is more threatened, as President Trump has issued an executive order to halt new offshore wind leases and permits in federal waters.
- **Other renewables**: Geothermal, biogas, and hydroelectric power are less politically sensitive. "Advanced" geothermal projects leverage advances in subsurface modelling and horizontal drilling learned from the natural gas fracking boom to generate clean baseload power. Future water management projects could involve hydroelectric opportunities.
- **Upgrading grid infrastructure**: Like Europe, US grid infrastructure needs significant upgrades in many parts of the country, with transmission lines and transformers operating well beyond their intended lifespan.
- **Nuclear revitalisation**: Driven by demand for clean firm power, operators of three shuttered US nuclear reactors have announced plans to restart their facilities, including a multi-billion dollar commitment from Microsoft to reactivate Three Mile Island in Pennsylvania.

CASE STUDY

NATURAL GAS POWER PLANT[5]

Funds advised by IFM provided debt financing to an 805 MW natural gas power generating plant in the Mid-Atlantic region of the US. The business benefits from higher capacity pricing driven by increasing demand for US power and the need for reliable dispatchable resourcing by the grid operator. Domestic capacity has historically priced at a premium due to imported power limits, transmission constraints, and difficulty constructing new plants. This is expected to continue as load growth and asset retirements tighten reserve margins on the grid.

We believe the business is well positioned to benefit from the forecasted energy demand growth driven by factors including increased EV adoption rates, higher data centre growth, and some building electrification assumed in New Jersey. To date, the business has benefited from conservative leverage, a track record of operations, a robust hedging strategy and experienced equity ownership.

[5] Case studies are provided for illustrative purposes only and should not be relied on to make an investment decision.

PROTECTING DRIVERS OF GROWTH: THE DIGITAL ECONOMY AND ADVANCED MANUFACTURING

As debt investors, we are keenly focused on protecting against downside risks. Understanding how growth plans can go wrong is important to our decisions to lend to infrastructure projects (such as rail, fibre, and data centres) supporting manufacturing growth. Even advanced manufacturing companies with significant government support have faced challenges, including Northvolt, the Swedish battery manufacturer that filed for bankruptcy last year. When investing in infrastructure to support growing industries, it is important to understand the competitive forces in an industry, and the strength of the contracts and offtake agreements manufacturing companies are able to secure.

We see opportunities to invest in the following infrastructure assets to support domestic technology and manufacturing development.

Data centre development: This is at the top of the agenda for countries striving to compete in the AI technology boom. The economics for data centres vary regionally, depending on factors like grid connectivity, land availability, local climate, and proximity to major tenants in technology hubs. Data centres are power-hungry and less sensitive to power prices than other users, which can lead to compelling opportunities to invest in the power plants tied to them. They also tend to benefit from highly rated counterparties with strong lease agreements.

Improved infrastructure in rural areas: Reshoring of manufacturing will likely mean factories and logistics infrastructure will need investment in more rural areas where there is sufficient land to build facilities. Digitisation has also created opportunities to invest in the fibre rollout in rural areas to replace less efficient copper wires.

Transportation infrastructure: If supply chains are being rerouted towards allies and trading partners, they will require better local and regional transportation infrastructure. Investment is also needed to electrify transportation to meet emissions reduction targets. We see opportunities to lend to businesses upgrading rail, bus, and ferry infrastructure to make it more efficient, sustainable, and able to handle increased capacity.

CASE STUDY

FIBRE-TO-THE-HOME[6]

Funds advised by IFM provided debt financing for the largest independent fibre-to-the-home operator in France. The business designs, owns and operates fibre network infrastructure across the country with a focus on low- and medium-density areas where current connectivity is more limited. Currently in France, one in five households lack access to reliable, high-speed internet.

The French government and regulator are very supportive of the provision of fibre networks and the decommissioning of the copper network throughout France to promote digital inclusion via a less carbon intensive source. Unlike many other European economies, the provision of fibre services in France is regulated. Each operator in France has access to the network at determined pricing guidelines and benefits from a permanent right of use of 5% of the network capacity in a given area for a 20-year period. Ultimately this limits the risk of overbuild or over-competition for the provision of fibre services in a given area, especially in low density areas where businesses benefit from subsidies to improve the provision of services.

[6] Case studies are provided for illustrative purposes only and should not be relied on to make an investment decision.

CONCLUSION

As the world becomes increasingly digital, we are witnessing economic change happening at a rapid pace. Global trade and mobility will remain important, but as governments seek to protect their domestic economies and improve global competitiveness, we expect to see more protectionist policies. Infrastructure will need to evolve to meet these changing economic needs.

Jacob Otto

Director, Head of Product Specialists – EMEA

Joined IFM Investors in 2021

Jake is Director, Head of Product Specialists for the EMEA region, where he leads a team that provides specialised support for both our infrastructure equity and debt client and prospective-client relationships. His team brings the best of IFM Investors' investment insights and content to conversations with our clients. During his 18 years in the investment management industry, Jake has been focused on public and private fixed income markets including infrastructure, government, credit, and currency working with clients across the globe. Prior to joining IFM, Jake worked at Wellington Management and Income Research + Management.

changes in environmental and planning laws and regulations, and other governmental rules; environmental claims arising in respect of infrastructure acquired with undisclosed or unknown environmental problems or as to which inadequate reserves have been established; changes in energy prices; changes in fiscal and monetary policies; negative economic developments that depress travel; uninsured casualties; force majeure acts, terrorist events, under insured or uninsurable losses; and other factors beyond reasonable control.

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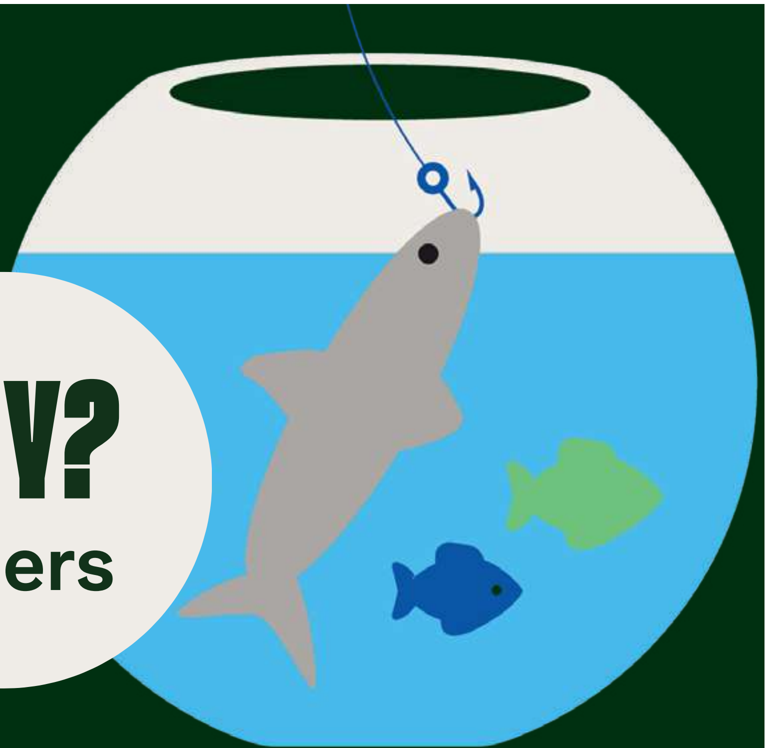
BC Securities Commission
Invest Right



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  West Vancouver, B.C.
  V7V 4S4

Report online:

Analyzing CMHC's 2025 Canadian Housing Market Outlook

*by **Justin Smith,** President*
Hawkeye Wealth

The Canadian Mortgage and Housing Corporation ("CMHC") has published their 2025 Housing Market Outlook Report, and as we predicted in our May 2024 article, it appears that they significantly overestimated the pricing forecasts that they set up 9 months ago. Admittedly, the tariff situation that Canada is facing was a new wrinkle for the market, so we don't fault them for not taking them into account, but their overestimation of immigration from 2024 onwards was foreseeable.

The result is that in the 2025 Housing Outlook, CMHC has significantly reduced their housing price and rental rate forecasts versus what was projected in 2024, but in our view, they may not have revised far enough.

In this edition of the *Bird's Eye View*, we share the key findings from CMHCs 2025 Canadian Housing Outlook, compare how and why their forecasts changed between 2024 and 2025, and give our perspective on whether their updated forecasts are likely to be accurate.

HOW DID THE FORECAST CHANGE?

In the charts below, we briefly summarize the key changes between the 2024 and 2025 Housing Outlook forecasts:

Resale Market (Canada-Wide)	2024 Average MLS Price Forecast	2025 Average MLS Price Forecast	2026 Average MLS Price Forecast	2027 Average MLS Price Forecast
2024 Housing Outlook	$711,429 (4.9% annual increase)	$779,357 (9.5% annual increase)	814,851 (4.6% annual increase)	N/A
2025 Housing Outlook	$687,100 (actual, 1.3% increase)	$729,200 (6.1% annual increase)	749,600 (2.8% increase)	770,100 (2.7% annual increase)

Rental Market (Vancouver)	2024		2025		2026		2027	
	Vacancy Rate	Average Rent 2 Bedrooms	Vacancy Rate	Average Rent 2 Bedrooms	Vacancy Rate	Average Rent 2 Bedrooms	Vacancy Rate	Average Rent 2 Bedrooms
2024 Housing Outlook	0.8%	$2,380 (9.1% annual increase)	0.9%	$2,580 (8.4% annual increase)	1.0%	$2,800 (8.5% annual increase)	N/A	N/A
2025 Housing Outlook	1.6%	$2,314 (6.1% annual increase)	2.1%	$2,461 (6.4% annual increase)	2.4%	$2,605 (5.9% annual increase)	2.9%	$2,758 (5.9% annual increase)

Source: 2024 and 2025 CMHC Housing Outlook Reports, data compiled by Hawkeye Wealth

We will dive into the reasoning in the next section, but the short answer is that CMHC has cooled their resale and rental market expectations across the board, with projected housing price increases getting chopped in half, vacancy rates rising, and lower rates of rental price increases.

That said, I think most investors would still be thrilled with these outcomes given the level of uncertainty ahead.

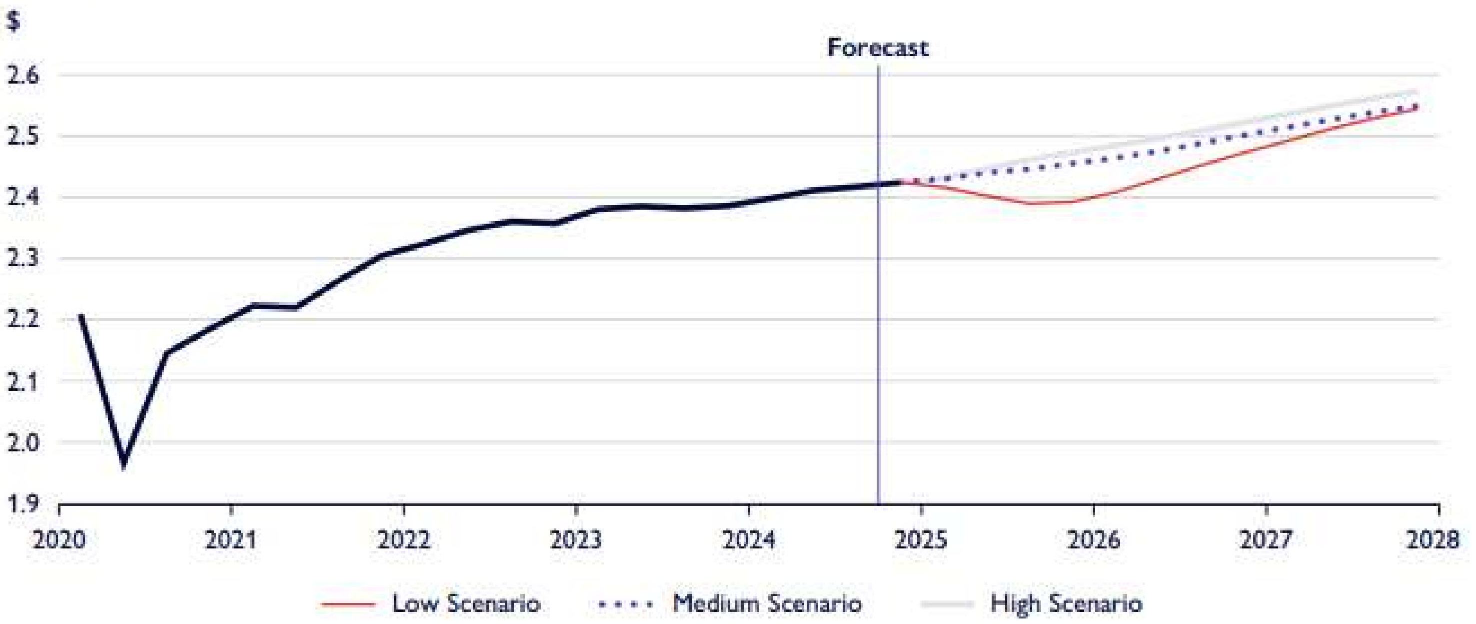
The question is, how likely is CMHC to be right?"

CMHCS FORECAST RATIONALE

Economic Uncertainty

CMHC begins with a caveat that the forecasts in their report are subject to considerable uncertainty due to foreign trade risks, and that they've modelled a 'low', 'medium', and 'high' scenario based on the size and duration of tariffs over the next few years.

Figure 1: Canadian economy faces significant uncertainty
Canada Real GDP Forecast (trillion $CAD)



Source: CMHC
The forecasts included in this document are based on information available as of January 14, 2025.

Source: 2025 CMHC Housing Outlook Report

While CMHC doesn't expressly hold out any of these 3 scenarios as being the one they see as most likely, for the purpose of our analysis and for comparison between the 2024 outlook and the 2025 outlook, all figures in this article reference the 'Medium' scenario.

Lower Housing Starts

> *"We expect housing starts to slow down over the forecast period, remaining above their 10-year average. The slowdown is primarily due to fewer condominium apartments being built. With low investor interest and more young families looking for family-friendly homes, developers will find it harder to sell enough units to fund new projects. The increase in unsold units will likely reduce new project launches, leading to a decline in new condominium apartment construction."*

This finding is consistent with their 2024 forecast, and we generally agree with it.

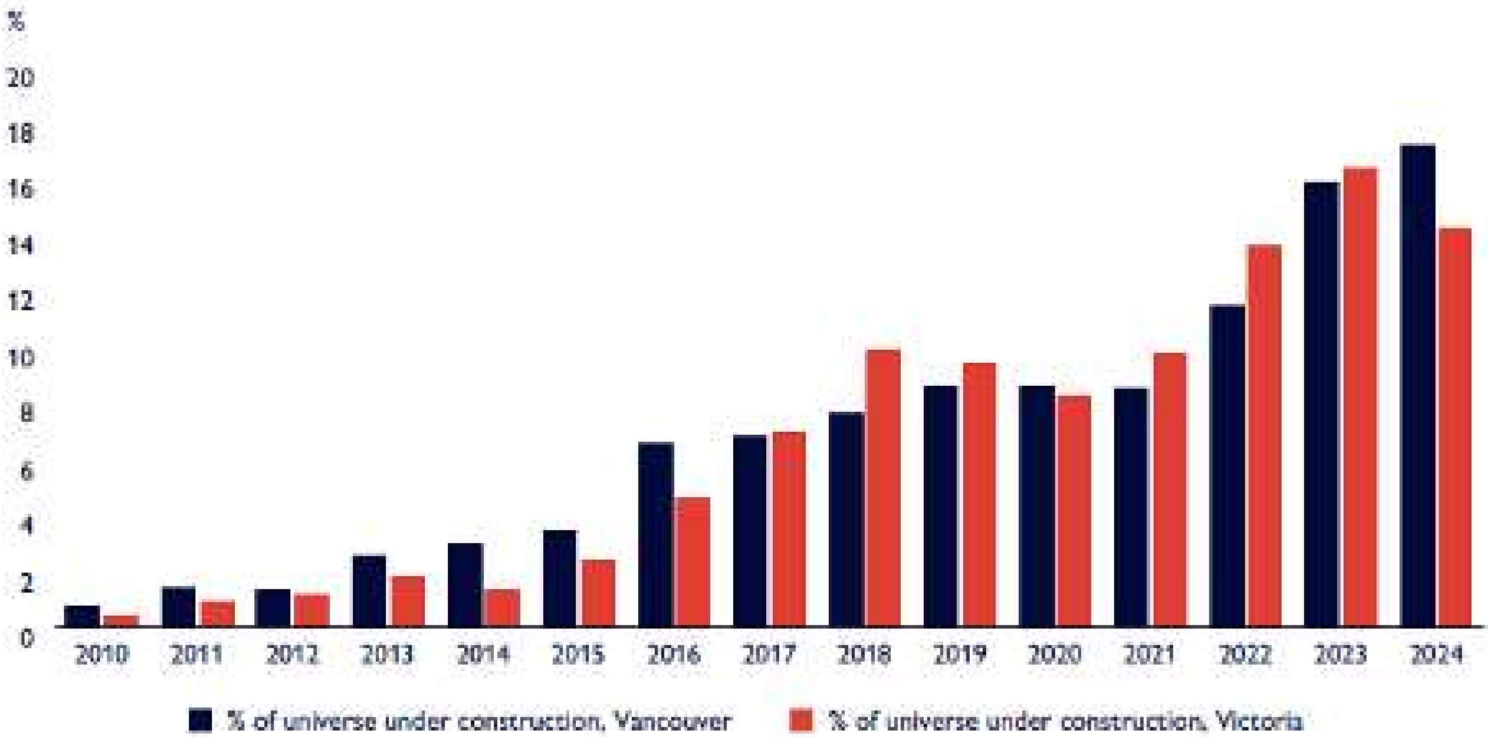
That said, we think they may be slightly overestimating the level of new housing starts in some major markets, notably Vancouver and Toronto, as it doesn't appear that CMHC is fully considering the tapering of new purpose-built rental projects that has already begun.

CMHC accurately showcases the massive wave of purpose-built rental projects that are currently under construction (see chart below), but they primarily use it as support for their assertion that "asking rents and rents of new units [will] have limited growth" (Page 11).

Frankly, we think that assertion feels crazy in circumstances where they are projecting out ~6% rental rate increases for the next three years, but putting that aside, they don't appear to go one step further to consider how the massive backlog in purpose-built rental projects, combined with lower population growth rates may further deter developers from starting these projects.

Figure 2 : Influx of Rental Supply Will Impact the Market in the Near Future

Purpose Built Rental Universe Supply and Under Construction



Source: CMHC

This chart shows that as of the end of 2024 in Vancouver, a whopping 17.2% of all purpose-built rental units in Vancouver were currently under construction. This is an all-time high figure, and will put downward pressure on rents as inventory comes online. The prospect of high land costs, high construction costs, regulatory and tax hurdles, lower immigration, and an influx of supply has developers looking elsewhere and to other asset types.

Our prediction: CMHC gets it right that housing starts are lower, but that they overestimate the number of new starts in each of 2025 and 2026. One potential caveat would be if the government dramatically reduces development fees, which would lower costs and give developers the confidence to proceed despite lower prospects for rent growth or appreciation.

Home Prices Up

> *"We expect housing sales and prices to rebound as lower mortgage rates and changes to mortgage rules unlock pent-up demand in the short term. In the longer term, stronger economic fundamentals will support this rebound."*

CMHC's underlying thesis for higher resale prices is that the reduction in immigration demand will have less impact on housing than on rentals, and that lower mortgage rates will prop up housing prices.

It seems like an odd time to be projecting out 'stronger economic fundamentals' for 2026 and 2027, but maybe that's just us?

Our prediction: We think that there is less pent-up demand in the market than what CMHC projects, and that fears of economic downturn will prevent large housing price increases in 2025. We see it as unlikely that housing prices rise by the 6.1% forecast for 2025, but feel that their 2026 and 2027 price growth rates are more reasonable.

Rents Keep Climbing

> *"A record number of units are under construction as part of efforts to increase rental supply... As more new, higher-priced units come onto the market, average rents will continue rising. However, we expect asking rents to be negatively pressured as rental demand declines."*

In this report, CMHC doesn't give Canada-wide rental forecasts, only regional forecasts. As such, we focus on the Vancouver rental market in this article.

CMHCs rationale for three years of ~6% rental price increases feels incredibly weak, even if they did adjust downward somewhat from their 2024 predictions. Yes, the wave of new units that come onto the market will be priced above current averages, and given the size of that wave, it will have a noticeable effect. However, even before any economic weakness that stems from potential tariffs, demand is already falling and will continue to do so as plans to slow immigration kick in.

Our Prediction: CMHC is overestimating rental price increases, as they continue to underestimate the slowdown in demand and the cooling effect of new supply. In our view, we anticipate flat or low rental growth rates in Vancouver, and believe that negative rent rates are a real possibility over the next couple of years.

WHAT DOES THIS MEAN FOR INVESTORS?

CMHC continues to paint an optimistic picture for investors in the BC housing market, but in our view, the data is leading us to believe a more bearish stance is prudent when underwriting...

At the least, investors will want to make sure that potential investments will still yield acceptable returns in a lower growth environment than what CMHC has projected.

In the meantime, we continue to look at deals on both sides of the border. While we believe many markets in Canada are in for some turbulence, we are more bullish on U.S. multifamily (see our last article), where a number markets are seeing new supply dwindle and rents are starting to grow again.

Justin Smith
President, Hawkeye Wealth

Before settling down in the Lower Mainland in 2009, Justin called many cities home, including Williams Lake, Quesnel, Kelowna, Montreal, Quebec City, and Edmonton. He is the third of six children (five boys and a girl), an environment he credits for any interpersonal and peacemaking skills.

Justin obtained his Bachelor of Arts in Psychology at the University of British Columbia prior to pursuing an MBA at Simon Fraser University where he met his wife, Elaine. Shortly after completing his MBA, Justin began his career in real estate, working with the largest residential developer in Northeast BC. In 2014, Justin saw the opportunity presented by the 2008 recession in the US and started helping investors participate in value-add apartment building deals across Arizona, Texas, and Georgia, which proved very profitable.

In 2017, he created Hawkeye Wealth with an aim to widen the scope of quality offerings for his investor network, primarily focusing on industrial and residential developments in Western Canada and the US, as well as mortgage funds.

Justin lives in South Surrey with his wife Elaine and son Grayson. When not at work, he enjoys improving his "low and slow" barbecue skills and is an avid Toronto Raptors fan. He is also fluent in Spanish, having spent two years volunteering in Spanish-speaking communities in Quebec.

British Columbia: Budget 2025

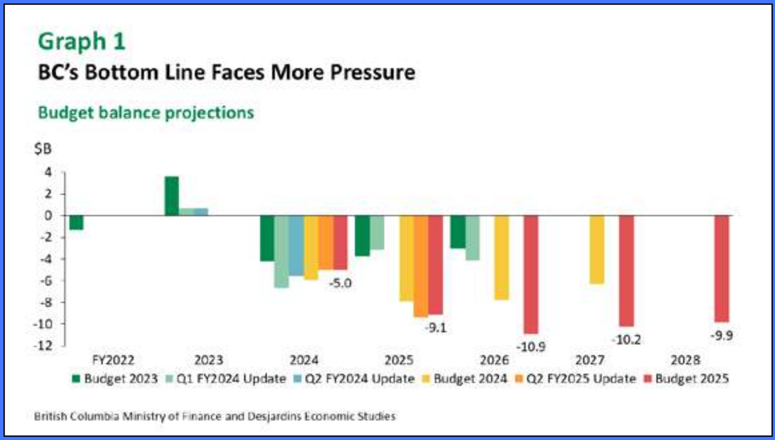
A Prudent Plan for a Turbulent Time

*by **Laura Gu,** Senior Economist and*
***Kari Norman,** Economist*

Desjardins
Global Asset Management

HIGHLIGHTS

- British Columbia's fiscal year 2025–26 (FY2026) budget reveals deeper-than-anticipated deficits under prudent assumptions, while preparing for strong fiscal headwinds blowing from south of the border. The provincial government is now projecting a $10.9B deficit in FY2026 which gradually narrows to $9.9B in FY2028 (graph 1). Table 1 on page 2 summarizes the province's updated fiscal forecasts.



- The updated fiscal plan is characteristically prudent, as the province continues to embed ample buffers through contingencies and conservative assumptions.
- The government's estimated downside risks from new US tariffs, which could result in additional annual shortfalls ranging from $1.7B to $3.4B due to pervasive job losses and reduced corporate profits, appear reasonable.
- Amid the financial strains caused by US tariffs, the province has managed to control spending by keeping new policy measures light and targeted.
- Larger projected deficits are expected to push the debt-to-GDP ratio higher from 22.9% in FY2025 to 34.4% in FY2028. Gross borrowing requirements are now expected to total $31.1B in FY2026, $33.1B in FY2027, and $34.7B in FY2028. For FY2026 and FY2027, the updated borrowing requirements represent a total increase of $6.2B from last year's budget.
- In light of a weaker revenue outlook and significant tariff impacts, BC's Budget 2025 balances critical investments with a relatively manageable debt position, even as the province's debt is expected to rise as a share of the economy. By keeping program spending increases incremental and targeted, despite strong revenue headwinds from external factors, the budget is a step in the right direction, paving the way for further consolidation in future plans.

OUR TAKEAWAYS

Anticipating strong headwinds to its bottom line from external factors—a common theme across all provinces this budget season—BC tabled a prudent plan that projects deeper-than-anticipated shortfalls over the planning horizon. With new spending kept incremental and targeted, weaker revenue growth is expected to drive a deeper deficit of $10.9B in FY2026, gradually narrowing to $9.9B in FY2028.

ACCOUNTING FOR THE TARIFF IMPACT

BC lowered its forecasts for economic growth this year and next in its base case to reflect lower population growth assumptions. The budget projects BC's economy to grow by 1.8% in real terms in 2025 and 1.9% in 2026, slightly below the first quarter update projections of 2.0% in 2025 and 2.3% in 2026, and in line with average private-sector growth forecasts.

The government provided an alternative scenario that accounts for the impact of US tariffs, assuming 10% tariffs on Canadian energy exports and a 25% tariff on all other goods, along with partial retaliation from Canada. The scenario sees real GDP growth slow to 0.3% in 2025 and 0.8% in 2026, potentially leading to annual revenue reductions ranging from $1.7B to $3.4B over the planning horizon.

The downside risks outlined in the alternative scenario are reasonable in our view. While the province faces similar challenges as the rest of the country due to US tariffs, BC's diversified export destinations offer some protection. The province otherwise expects solid growth this year as interest rates decline and fiscal policies remain stimulative. LNG Canada is set to boost natural gas exports from Western Canada when it begins commercial operations in mid-2025. Rising natural gas prices also bode well for BC.

The budget allocates substantial contingencies of $4B annually for the next three years. These contingencies help absorb unforeseen costs, such as a new collective-bargaining mandate and tariff impacts, and could potentially result in narrower deficits than planned.

TAX REVENUES TO ENCOUNTER NEAR-TERM HEADWINDS

The province foresees near-term pressure on its topline revenue growth, driven by lower revenues from corporate income taxes. Corporate income tax revenue is projected to decline by 24.8% in FY2026 and by an additional 8.5% in FY2027, before rebounding with a 12.2% increase in FY2028. Meanwhile, the personal income tax revenue projection remains intact and is expected to grow steadily, averaging 4.5% annually over the next three years, offsetting some of the short-term weaknesses in corporate income taxes (graph 2).

Graph 2
Solid Personal Income Taxes Offset Weaker Corporate Income Taxes

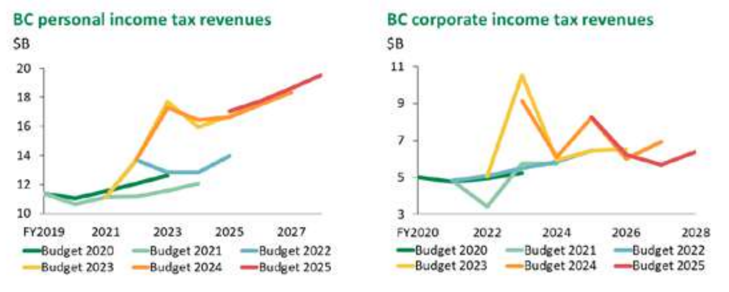


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TABLE 1

Updated BC Fiscal Forecasts

IN $B (UNLESS OTHERWISE INDICATED)	2023–2024	2024–2025		2025–2026		2026–2027		2027–2028
	Actual	**Q2 FY2025**	**Budget 2025**	**Budget 2024**	**Budget 2025**	**Budget 2024**	**Budget 2025**	**Budget 2025**
Total revenues	79.6	81.4	82.9	82.8	84.0	86.4	85.7	88.2
% change	*-2.3*	*2.3*	*4.1*	*1.7*	*1.4*	*4.3*	*2.0*	*2.9*
Own-Source Revenues	65.9	67.1	68.7	67.9	68.7	71.7	70.8	73.6
% change	*-4.5*	*1.9*	*4.2*	*1.2*	*0.1*	*5.6*	*3.1*	*3.9*
Federal Transfers	13.7	14.3	14.2	14.9	15.3	14.7	14.9	14.6
Total expense	84.7	90.9	92.0	90.6	94.9	92.7	95.9	98.0
% change	*4.7*	*7.3*	*8.7*	*-0.3*	*3.2*	*2.3*	*1.1*	*2.2*
Program spending	81.4	86.5	87.6	85.8	89.9	87.0	90.0	90.9
% change	*4.4*	*6.3*	*7.7*	*-0.8*	*2.5*	*1.4*	*0.1*	*1.0*
Debt charges	3.3	4.3	4.4	4.8	5.1	5.7	5.9	7.2
% of total revenues	*4.1*	*5.3*	*5.3*	*5.8*	*6.0*	*6.6*	*6.9*	*8.1*
Forecast allowance								
Budget balance	**-5.0**	**-9.4**	**-9.1**	**-7.8**	**-10.9**	**-6.3**	**-10.2**	**-9.9**
% of GDP	*-1.2*	*-2.2*	*-2.1*	*-1.8*	*-2.5*	*-1.4*	*-2.2*	*-2.0*
Net Debt, % of GDP	*18.4*	*22.3*	*22.9*	*24.8*	*26.7*	*27.5*	*30.9*	*34.4*
Gross Borrowing Requirements	**—**	**—**	**29.2**	**29.5**	**31.1**	**28.4**	**33.1**	**34.7**
Capital Requirements	13.4	17.6	16.0	19.0	20.2	18.7	20.4	19.3
Refinancing Requirements	—	—	3.8	6.3	8.2	6.3	6.3	8.8
Other Financing Sources	—	—	0.5	-3.3	(7.4)	-2.6	(3.4)	(3.2)

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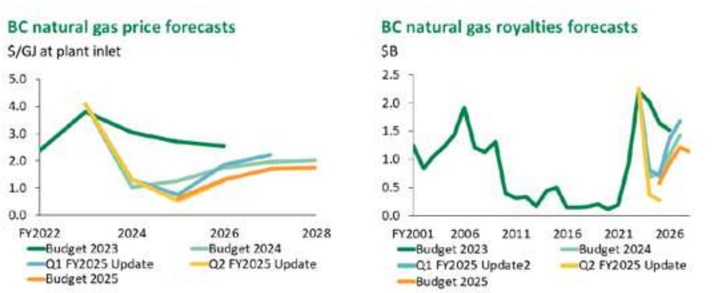
NATURAL GAS SUPPORTS REVENUE GROWTH WITH ROOM FOR UPSIDE

Revised down from the province's first quarter update, natural gas royalties forecasts continue to be underpinned by conservative natural gas price assumptions well below the average of private-sector forecasts (graph 3). The updated fiscal plan projects average royalties growth of 26% per year over the next three years due to higher prices and production volumes, with potential for more upside if momentum in natural gas prices persists.

Graph 3

Conservative Natural Gas Price Forecasts Provide a Buffer



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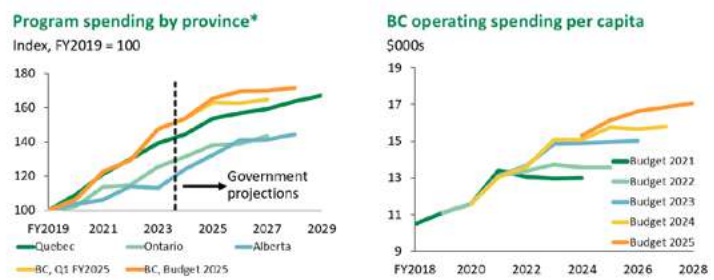
LIFTED NEAR-TERM SPENDING TARGETS HEALTHCARE

Program spending has been lifted although increases appear moderate (graph 4). It's now projected to rise by 2.5% in FY2026—a reversal of the previously planned spending cut but it's still a reasonable pace consistent with inflation plus population growth. Outer-year spending growth was kept under an average of 0.6% annually, leading to a gradual reduction in deficits.

Graph 4

BC's Spending Plans Continue to Grow



* Quebec and Ontario figures based on mid-year FY2025 projections
Statistics Canada, provincial budget documents and Desjardins Economic Studies

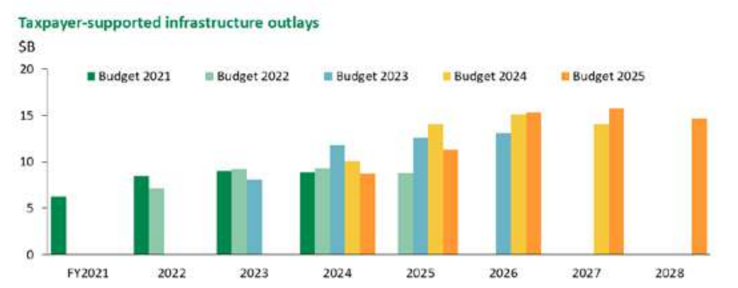
At $4.2B, healthcare-related investments make the largest contribution to the $9.9B in additional expenses across the three-year horizon. This builds on the significant health and mental health spending outlined in the province's previous plans. New spending outside of healthcare has been kept incremental, with a focus on education and social services.

On a per capita basis, program spending is projected to grow as the province anticipates stagnant population growth throughout the planning horizon. The government expects BC's population to increase by 0.2% in 2025, before declining by 0.3% in 2026, lower than our updated forecast.

INCREASED CAPITAL OUTLAYS AND DEFICITS ELEVATE BORROWING NEEDS

Capital spending was lower in FY25 ($11.3B) than planned in the first quarter update ($13.6B) but will rise to $15.8B in FY26, totalling $45.9B over the three-year horizon (graph 5). The increased infrastructure investments aim to stimulate economic activity amid US tariff challenges but will also contribute to a higher net debt burden. Over 60% of the spending will be allocated to projects in public transit and healthcare. The capital plan is anticipated to support 180k jobs in the province over three years.

Graph 5
Major Capital Spending to Stimulate the Economy



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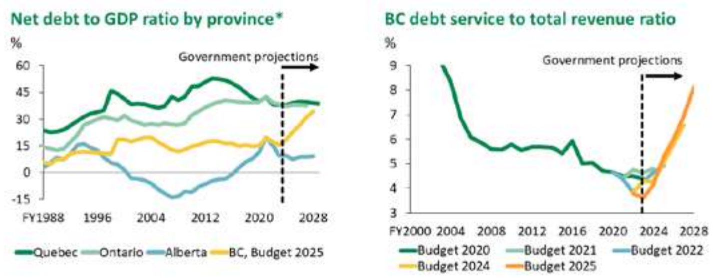
Net debt is projected to increase as a share of nominal output, rising from 22.9% in FY2025 to 34.4% in FY2028. This should remain well below the levels of Ontario and Quebec (graph 6 on page 4), which have yet to announce their updated fiscal plans. As the government continues to forecast rising debt levels, debt service costs are expected to rise from 5.3% of revenue in FY2025 to 8.1% in FY2028. These estimates likely represent an upper bound, given the substantial prudence embedded over the planning horizon.

Graph 6
BC's Debt Indicators Are Set to Rise, But Remain Favourable



* Quebec and Ontario figures based on mid-year FY2025 projections
Provincial budget documents and Desjardins Economic Studies

Borrowing requirements have been revised upward to $31.1B in FY2026, compared to the previous forecast of $29.5B in the last budget, driven by higher refinancing maturing short-term debt with long-term borrowing. For FY2027 and FY2028, the province expects to borrow $33.1B and $34.7B, respectively, reflecting higher capital spending projections and a deeper deficit outlook.

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