

EP 206 | Quarterly Update Q4 2025



[00:00] Kevin Minas: On this episode of the Art of Boring, I sit down with Stu Morrow, an investment counselor here at Mawer. Stu and I are looking back at an eventful fourth quarter of 2025, including what the macro data really told us, how central banks and bond markets reacted, and what that meant for credit markets. We'll also dig into the changing shape of equity leadership in an AI-obsessed market and what the developments in Venezuela and the energy complex might mean for portfolios.

Finally, we'll bring it together with how we're positioned across our balance portfolios as we head into 2026.

[00:37] Disclaimer: This podcast is for informational purposes only. Information relating to investment approaches or individual investments should not be construed as advice or endorsement. Any views expressed in this podcast are based upon the information available at the time and are subject to change.

[00:53] Kevin Minas: Welcome to the podcast, Stu.

[00:55] Stu Morrow: Thanks, Kevin.

[00:56] Kevin Minas: So, I think it's your first time on the podcast.

[00:58] Stu Morrow: It is. Long time, first time.

[01:00] Kevin Minas: Fantastic. We are doing the quarterly today. Between you and I, we'll cover the big macro themes, rates, credit, of course equities, and then asset mix. Why don't we start with you to set the stage. Big picture and global economy.

When you look at Q4 macro data, whether it be growth, inflation, or the labor market, what in particular stood out to you? How did that backdrop affect the opportunity set for investors?

[01:25] Stu Morrow: Big picture stuff. In Q4, we saw an ongoing mix of modest growth, softer labor conditions, and easing inflation. The U.S. economy stayed in a resilient but slowing mode.

Capital spending was held up thanks to AI-related investments and fiscal spending, but housing and hiring stayed a little weaker. The Fed's Beige Book [Federal Reserve] description of flat activity during the quarter, I think, captured the tone pretty well. One thing that continues to stand out to me, with just how much fiscal support remains in the system, is that government spending continues and debt keeps accumulating well past the COVID period now.

It's not just the U.S. We saw continued stimulus out of most G7 countries - Germany relaxing its fiscal brake, Canada's infrastructure-heavy budget, and most recently, we've seen Japan also leaning more supportive.

Here in Canada, bringing it back to growth, third-quarter strong headline GDP of 2.6% annualized, masked some of the underlying weakness. Data during the quarter did show softer domestic demand, weaker consumption, and declining business investment. On the inflation front, globally, inflation seems to have been evolving as central



banks expected. Still above target in some economies but drifting lower, especially as energy prices cooled as we exited the year and services inflation eased as well.

On the labor front in North America, the market softened but hasn't cracked. The U.S. showed slower job growth and a modest rise in unemployment into December, while here in Canada, the latest Labor Force Survey showed rising unemployment, and muted hiring, despite a few strong monthly prints.

Getting back to your question about the opportunity set, I think against that backdrop we certainly did see global equity markets had another strong quarter. Tariffs, geopolitical events, and doubt about some of the continuation of the AI trade benefited some non-U.S. markets. Easier global policy also supported equities. Canadian stocks had a solid finish to the year, helped by strengthened metals and mining and good results from the Canadian financials.

When I think about the fourth quarter in 2025, the results from the economy and the markets seemed at times to move on different schedules. It is always a good reminder that markets do trade on expectations, policy earnings and sentiment often before the data confirms it.

That's a big macro picture. Studies of declining inflation, decent activity, and markets are already looking forward. Of course, none of that happens in isolation, and central banks were a big part of that story in Q4.

Kevin, how do the markets and central banks respond to that evolving mix of growth and inflation? What do we see in terms of bond market performance?

[04:07] Kevin Minas: I would say for the quarter, as well for 2025 overall, the key story for bond investors, and central banks particularly, was really about the move of central banks from how restrictive to how to normalize. We saw a lot of cutting throughout the year. Markets responded quite favourably to that.

Starting in the U.S., you've got the Fed that cut three times in 2025, twice in the quarter, at both the October and December meetings. That brought the Fed funds rate down to a range of 3.50-3.75%, however those decisions were not unanimous.

If you look at the December decision, the Fed vote was nine to three in favor of a cut, which does indicate, to your point earlier, that there is still some debate around inflation and whether core inflation remains above target. There are some dissenting voices as to whether we should really be in a cutting cycle, but that 3-3.5% is still at a restricted level, still within a restricted range.

I think that was sort of the key rationale for why you got the cuts. The direction of travel does appear to be pretty clear in terms of lower rates. From the Fed, as you mentioned before, you have a soft labor market, job openings and quit rates back to 2021 levels.

That has really tilted the risk balance in favour of further easing. Notwithstanding what we've seen since the end of the quarter with Jerome Powell, Federal Reserve Chair, and President Trump and all that noise, the direction of travel - certainly if it were in Mr. Trump's purview - would be to cut further. Even so, I think there are still reasons for the Fed to be in easing mode.

In Canada, you've got the Bank of Canada that moved 25 basis points in the quarter. Recall, the Bank of Canada has already been cutting. They started earlier and they've been cutting more aggressively. That brought the overnight rate to 2.25%, and unlike the Fed, they are already in pretty accommodative territory at the lower end of the range that the central bank targets. Financial conditions have already started to revert to those early 2020 levels.



You do have big uncertainties around, of course, U.S. trade and USMCA, which is due for renewal. The Bank of Canada signaled that they are happy and comfortable with the pause. They think the policy levels are about right, but you could certainly see further cuts if weaker data were to continue or some of these trade negotiations take a turn for the worse.

In terms of bond market reaction, particularly over the year, policy shifts have affected the curve quite a bit. In both Canada and the U.S., you've got the front-end rallying, short policy rates falling and that affecting short bond prices with longer yields moving less. As a result, you've got a steeper yield curve over the course of the year.

For our strategies, that was favorable, as our Canadian bond strategy was in a steepener position, meaning it would do well if longer yields underperformed relative to the short end, which is good for the strategy.

Lastly, in Canada, at the index level, you did see in the quarter a little bit of negative returns. That was really a function of the 10-year part of the curve in particular, where we saw yields move from about 3.2% to roughly 3.4%. There was a little bit of pressure on prices, even though you did see the steepener overall for the year. That led to okay results in the quarter and it was reasonable results for the year as well.

Credit was another theme that did quite well. Speaking of credit, how would you say both investor grade and high-yield markets behaved in Q4, both in terms of spreads and any colour on issuance? Where do we see the balance of risk and reward in corporate bonds as we head into the new year?

[07:32] Stu Morrow: In Q4, we saw global investment-grade and high-yield credit post positive returns. Most of that was derived from coupon income rather than spread tightening, as spreads were broadly stable throughout most of the quarter.

On the issuance side, activity did pick up. U.S. investment-grade supply ran higher than last year. A big driver there was tech-related borrowing from most of the hyperscalers—Amazon, Google, Meta, and Oracle—who tapped the market to fund AI infrastructure. We also saw some issuance in financials and utilities.

Looking ahead, tech-related financing is likely to remain a dominant theme in credit markets into 2026 as demand for AI and data infrastructure continues to grow. That could put some modest upward pressure on spreads, and it is worth noting, are still sitting at multi-decade lows. The balance of credit markets today are still favoring borrowers over lenders. If growth does hold up, credit may continue to fund the AI spending, and potentially a pickup in corporate mergers and acquisitions, however we're cautious on how long that equilibrium does last.

I suppose the message to investors heading into 2026 remains much as it was in 2025: resist the urge to reach for yield, whether that means going down in quality, out in duration, or into less liquid markets. Obviously, we cannot time the turn in spreads, but we do believe it will come and the right playbook is to plan ahead. Protect capital now and be ready to deploy when that next credit dislocation inevitably presents itself. That is where we are in credit.

Turning it back to you, Kevin, thinking about the equity side, much of the story last year was dominated by that handful of mega cap growth names. Are we still seeing that concentration carry markets or did leadership finally start to broaden out in the fourth quarter?

[09:21] Kevin Minas: I would say more in the latter. It did start broadening out. AI was still a very dominant narrative, but as you mentioned off the top, at the headline level global equity markets had another strong quarter. What shifted a little bit was who led.



You had investors at the margin starting to rotate away from that narrow group of U.S. mega-cap AI winners. In the quarter, some of them did okay and some of them not so much. Overall though, a very strong year. There was a bit of a pullback in some of the hyperscalers. For example, Microsoft had driven a lot of the prior advance throughout the year. You did see a bit of a rotation into other areas that are more cyclical, whether it be small caps and also some rate sensitive areas of the market.

Having mentioned banks, that would be a good example of where we did see a rotation. We did see a bit of a broadening with Canadian equities specifically outperforming the U.S.

That was led largely by commodities, particularly gold. That's been a dominant theme in the market for a little while now, so no change there necessarily. European markets also did quite well and substantially outpaced the U.S. They have fairly large banking exposure, which helped with the yield curve. There is also some commodity exposure that also did quite well. On the AI front, I would say the conversation has shifted.

Earlier in the year, the focus was really on computing power and model leadership, the actual LLMs [large language models]. By Q4, there was a lot more attention on data center profitability, power supply constraints and the sheer scale of CapEx required. Even though this had already started earlier in the year, I think it was much more pronounced in the last quarter.

You talked about this a little bit in the credit section, saying that there is a lot of credit being taken out by these hyperscalers. In some ways, you can't blame them, since credit is pretty cheap right now. It might end up being a good return on investment for them, or maybe not. We will see, but the financing has certainly been quite attractive.

All of that has collectively raised more explicit concerns around talks of bubbles and parallels that have been drawn to previous technology booms, whether you go back to the railroads or something more recently like the dot-com era. There are some similarities, whether it be easy credit or increasing leverage, even retail participation, certainly stretched valuations, and the general concern about a correction in a lot of those pockets of market. I would say that there is sort of a nuanced view when it comes to AI, specifically.

What you did see in the quarter, which was a bit of a bifurcation, is AI enablers continuing to do well. These would be things like high-bandwidth memory, such as the South Korean company SK Hynix; TSMC, by far the world's largest semiconductor manufacturer; Kingslide; and Hitachi that does power. They've all continued to benefit from the explosive growth that you've seen on AI-related infrastructure, so they've continued to win.

Some of those hyperscalers that I alluded to earlier did pull back a little bit after a strong run. Even in the Canadian context, you have a couple of examples, such as software compounders like Constellation and Topicus, that have been facing questions around whether AI would disrupt some of their core offerings.

To bring it all together, and to answer your question directly, AI was still a key driver of equity markets in the quarter, but it wasn't the only driver. We did see some other parts of the market do quite well, which I think overall is quite constructive. If you're a long-term active investor, you want to see a little bit more breadth and diversification, as opposed to a very narrow part of the market where, if you want to stay diversified, arguably you would be overallocated if you're really focused on what's won over the last couple of years.

We see some of that broadening out, and I think that's a healthy adjustment. Maybe I have a question for you that relates to something that happened slightly past the end of the quarter, but I think it's such a big topic that it would be remiss if we were to ignore it. This relates to what we saw in the past week in Venezuela, where the U.S. intervention has really caught the market's attention.



Curious on your views and the team's views on the developments that have happened there. I know it's early, so it's difficult to get a read on this, but at least initial thoughts of what has happened, and particularly how it might impact oil markets globally and just the broader energy complex, in terms of the risks and opportunities that we're seeing at this early stage.

[12:25] Stu Morrow: It's never a dull moment in the world and markets, is it Kevin? There is always something. The U.S. intervention in Venezuela, as you said, certainly grabbed market's attention.

At this stage, it looks more like the start of what could be a long or untidy geopolitical saga than any immediate shock to a global supply. Venezuela is still a relatively small producer today compared to its historical potential or output. The oil market also came out of last year in a surplus, so the initial move in crude has been modest.

We saw gold and silver react more sharply to the news, as people reach for those geopolitical types of hedges. For Canadian investors, I think the important angle here is the medium- to long-term path if Venezuela manages to bring meaningful supply back to the market.

If U.S. technology and capital does unlock significant additional Venezuelan production over many years, along with growth that's already happening in heavy and medium crudes in Guyana, Brazil, and Argentina, you could see that Western Hemisphere may become that more dominant, oversupplied base and putting a structural pressure potentially on Canadian crude oil as all those barrels compete into the U.S. Gulf Coast refineries.

If you step back, Venezuela looks potentially less like a one-off headline and more like part of a broader shift towards this transactional, spheres of influence type of world, moving away from a post-war era of globalization and soft power towards something maybe closer to modern mercantilism, where spheres of influence are working hard to secure access to energy and critical minerals.

In that context, moves like this are about securing supply lines. If it does happen, getting from here to there is likely to involve more volatility ahead, more policy intervention, and more headline risk. I think that is exactly the type of environment where remaining disciplined, diversified, and a valuation-driven approach matters more than ever. It is still the early days, and there is a lot to unpack there but it really does show how interconnected geopolitics and markets have become.

Now, let us take a step back from all of this. Kevin, over to you to think about asset mix today. Between equities, bonds, and cash, given everything we've talked about with policy, credit, AI, and energy, how are you thinking about that asset mix today?

[15:47] Kevin Minas: Yes, I would say the focus has really been on at the margin. These are not large adjustments, but at the margin, we have trimmed our equities in favor of bonds, a mix of cash, core bonds, as well as global credit. The rationale, as we have discussed throughout the year, is that valuations have been quite elevated.

The markets have obviously done quite well throughout the year, so they have continued to push higher from a valuation point of view, and we've trimmed into that strength. We continued doing that in the quarter, and not a huge adjustment but nevertheless, we did make a small trim.

Within equities specifically, we made a few shifts under the hood. We trimmed a little bit of Canadian small cap in favor of large cap, and that's consistent with a view that we've had for a while now, where the opportunity set in the large cap space is quite a bit more attractive than in small cap. You have just seen a lot of companies taken private and not as many IPOs in the Canadian small cap space. There is still opportunity there, but just at the margin, we think that that greater breadth that you get from the large cap space in Canada is quite attractive.



Also, we've increased our exposure to the U.S. markets, sourced from emerging markets, and to a lesser extent, sourced a little bit from international as well, but emerging market being the bigger one. If you recall, over the last 12 to 18 months, we'd actually made the opposite move. We were moving out of trimming the U.S. at the margin, partly a valuation story in favor of international and EM. Those markets have outperformed in 2025, so it was a good adjustment with the benefit of hindsight. However, as those markets' relative valuations have moved, we are now taking the opportunity to reverse some of that trade, peel back a little bit of that EM and international exposure, and then add it back to the U.S.

I mentioned that we trimmed equities and we put it into fixed income. The logic there, besides the rationale I've already given, is that the case for fixed income is that we still think the asset class generally remains pretty appealing. If you think about global central banks pivoting towards easing longer yields, they're still actually relatively elevated by historical standards. That zero-interest rate policy we were in for many years; we're out of that. Even though rates are coming down, starting yields are still decent.

During the macro section, you pointed out that we are starting to see, whether it be labour data or some of the other macro data, that there is a bit of a slowdown in the economy and that it is helpful to have a little bit more bonds than if you do get a risk-off scenario, hence the shift out of equities into fixed income. Having said all that, the balance strategy overall is sitting not too far off neutral, which we think does sort of reflect that rising valuation concerns have been lingering questions, really, about the state of the economy.

And so, all else equal, we think sort of a neutral posture is warranted at this point. That is all I have for today and I think this was a great first conversation. Looking forward to more in the future.

[18:36] Stu Morrow: For sure. Thanks for having me.

[18:37] Kevin Minas: Hey, everyone. Kevin here again. To subscribe to the Art of Boring Podcast, go to mawer.com. That's M-A-W-E-R.com forward slash podcast or wherever you download your podcasts. If you enjoyed this episode, be sure to leave a review on iTunes, which helps more people discover the Be Boring, Make Money philosophy. Thanks for listening.