NEI Conservative Yield Portfolio

Q1 2025 Commentary

NEI

Market review

Markets have undergone a significant shift in tone in the first quarter of this year, reflecting a broader regime change in the global economic landscape. The US economy is showing signs of weakening, with slowing consumer activity and a softening labor market, which has weighed on US equity performance. The market witnessed a rotation out of US assets and into international markets driven by high valuations in the US and ongoing tariff uncertainties. US equities underperformed both Canadian equities and the cheaper overseas markets during the period, a reversal of trend where “US exceptionalism” pushed equity markets to new highs. The “Magnificent Seven” also experienced a significant correction in the first quarter. The uncertainty has contributed to a risk-off tone, leading to a sector and factor rotation: economically sensitive sectors have lagged, while defensive areas—such as healthcare, consumer staples, and utilities—have outperformed. Similarly, low-volatility stocks and dividend-paying names have outshined small-cap and high-growth equities. In Canada, the materials sector had the strongest return, as gold reached a new record high.

The fixed income markets also navigated a volatile macro backdrop shaped by geopolitical tensions, tariff uncertainty, and diverging monetary policies. US Treasury yields had notable fluctuations, initially rising due to fiscal stimulus expectations under the Trump administration but later eased as inflation data softened and markets priced in further Fed rate cuts. Credit spreads widened moderately, reflecting resilience in corporate fundamentals, but investors remained cautious amid elevated inflation concerns and possible stagflation stemming from tariffs. Canada’s fixed income market delivered a strong start to 2025, driven by rate cuts from the Bank of Canada, as well as a flight to safety based on concerns about tariffs on Canadian goods. European government bonds posted mixed results, with German Bunds underperforming due to fiscal policy shifts, while UK gilts rebounded after inflation surprised to the downside.

Returns

Fund	3 months	6 months	YTD	1 year	3 years	5 years	10 years	Since inception*
NEI Conservative Yield Portfolio Series I	2.46	2.71	2.46	9.13	5.11	6.50		4.44
NEI Conservative Yield Portfolio Series A	2.02	1.82	2.02	7.23	3.30	4.66		2.83
NEI Conservative Yield Portfolio Series F	2.24	2.26	2.24	8.17	4.20	5.57		3.70
Benchmark 1: 75% Barclays Global Aggregate CAD Hedged, 18% MSCI ACWI, 7% S&P TSX	0.51	0.74	0.51	6.12	3.20	3.34		3.41

*Source: Morningstar. As of March 31, 2025. The benchmark since inception return in the table is calculated as of the inception date of Series A. Since inception benchmark returns for Series F and Series I are 3.38 and 3.4, respectfully.

On March 1, 2023, the fund benchmark was changed. Prior to this date, the fund benchmark was 80% Bloomberg Barclays Global Aggregate Index (C$ hedged), 14% MSCI World NR Index (C$) and 6% S&P/TSX Composite TR Index.

Performance

The Portfolio outperformed the benchmark in the first quarter as manager selection added positively to performance while out-of-benchmark allocation detracted and asset allocation had a minor impact. Within fixed income, Global Total Return Bond Fund added value as the overweight duration, country allocation and steepening bias contributed positively. Within equities the allocation the Global Dividend RS Fund was a significant contributor to performance due to its focus on low volatility and its value and dividend tilt – areas that outperformed in the first quarter. The US Equity RS Fund also outperformed its benchmark due to its focus on downside protection, although overall the allocation to this fund detracted from absolute performance.

Outlook

Recent market volatility has been largely driven by significant shifts in US trade policy, particularly the sharp escalation in tariffs. Historically, such rapid increases in tariffs have had considerable economic impacts, as seen during the 1930s with the Smoot-Hawley Tariff Act. The US is currently facing multiple challenges: a rising debt burden, growing interest payments, and a large fiscal deficit. These factors are driving the new administration to enact aggressive tariff policies as a means to generate income for potential tax cuts. However, this approach could lead to stagflation or recession. These developments can erode both consumer and business confidence and weaken economic growth.

We are actively monitoring these developments and evaluating a range of possible outcomes. The bear case scenario involves a deep recession with significant earnings cuts and valuation compression. The base case scenario anticipates continued uncertainty affecting valuations, leading to subdued but stable market performance. The bull case scenario hinges on a resolution of trade tensions and renewed focus on pro-growth policies which could drive a rebound in sentiment and equity prices.

It is uncertain which one of these scenarios will happen, however it’s clear that for investors, in light of these conditions, diversification across asset classes, geographies, factors, and styles remains crucial. Assets that have lower correlations with markets, higher quality investments, and income-generating assets are particularly important in this volatile environment. Alternative investments can provide a buffer against market swings and help stabilize portfolio returns. High-quality companies with pricing power and strong fundamentals, robust balance sheets, consistent earnings, and competitive advantages, are better positioned to withstand market fluctuations. Income-generating assets play a vital role in providing stable returns, especially in volatile or sideways markets. Both Canada and Europe currently offer higher dividend yields compared to the S&P 500 at the index levels, making them attractive options for income-focused investors.

In global markets, the outperformance of US equities has come with a growing valuation premium over other markets. While US earnings have been relatively strong, current valuations leave little margin for downside surprises. For some time now, our global equity managers have been increasingly looking for value in markets outside the US focusing on businesses with limited tariff exposure, strong local demand, and increased allocations to defensive sectors like healthcare and consumer staples.

For long-term investors, staying invested is crucial. Markets can rebound quickly—often faster than investors can reposition. Being out of the market during these turning points can be detrimental to reaching long term goals.

Our multi-asset strategies are designed to provide balanced exposure across various market conditions and mitigate the impact of volatility. These portfolios are carefully constructed to combine defensive positioning with exposure to attractive opportunities, aiming to deliver resilient, risk-adjusted returns.

In the latest strategic re-optimization of portfolios implemented in February of this year, the NEI Asset Allocation Team has made strategic shifts in anticipation of a more volatile environment this year, emphasizing stability and quality across the portfolios which has had a positive impact. Key adjustments included: adding to global dividend funds to increase income and reduce volatility, increasing allocation to opportunistic global bonds, and introducing certain ETFs for tactical flexibility and thematic alignment with long-term trends. The team continues to closely monitor market dynamics and believes that the portfolios are well-positioned to navigate the current evolving environment and for the long term.