The Home Country Bias

Installment 1 | February 2025

Sionna Investment Managers®

About the Home Country Bias Series

Canada's strengths are often overlooked because of our self-deprecating national spirit. But since the U.S. President first threatened tariffs on Canadian goods, there has been a surge in Canadian pride and patriotism. Canadians are showcasing their national spirit in different ways – from proudly flying the country's flag, to seemingly large-scale support for homegrown products and businesses by shopping Canadian.

Sionna has proudly invested in Canadian equities for more than two decades, so this change in sentiment sparked our investment team's interest. We're launching a new series – ***The Home Country Bias*** – to address questions investors may have as we continue to navigate through an uncertain environment. There are a lot of questions to cover, so let's dive into a couple that are top of mind right now…

Will the 'buy Canada' sentiment mean investors shift back to Canadian equities?

While the actions of investors are impossible to predict, there are several reasons why investors should consider a higher allocation to Canadian markets:

- **Size**: Canada is the world's fourth-largest equity market after the U.S., Japan and the U.K., and believe it or not, larger than China! Despite this, the MSCI World Index, a global cap weighted benchmark, holds only 3.0% in Canada as at January 31, 2025 (all squeezed down by the U.S. weight of 73.6%)*
- **History:** The Canadian stock market boasts a rare 125-year track record
- **Performance:** The Dimson, Marsh and Staunton global markets study consistently shows Canada offering above-average, long-term returns, with below-average risk**
- **Attractive Valuation:** The Canadian stock market trades at a significant discount to the U.S. on several valuation metrics, including P/E, P/BV and dividend yield***, and should be more defensive in a market decline
- **Home Country Bias:** Investing domestically tends to cost less in management and trustee fees, attracts no global withholding taxes, simplifies tax returns, offers simpler asset liability matching and requires no currency hedging

How will Trump's tariffs impact the market?

There is uncertainty in the market as President Trump's threat of tariffs on Canadian goods is weighing on most Canadians' minds. So, in this installment of *The Home Country Bias*, we chose to focus on an industry that's getting a lot of attention right now – autos – and dive into who will likely feel the impacts of Trump's proposed tariffs.

Canada, the U.S. and Mexico have a multi-decade long history of integration for car manufacturing and assembly; the 2020 United States-Mexico-Canada Agreement (USMCA) reinforced this integration. USMCA strengthened an already highly efficient supply chain that moves parts across borders as many as six times before a car is complete.

Ultimately, the proposed tariffs would increase costs for the original equipment manufacturers (OEMs). This is a highly competitive, global industry where profit margins are in the single digits, so increased costs would likely be pushed onto the consumer. Car prices are estimated to increase 6.5%, on top of the 20% increase experienced after the COVID-19 pandemic. Demand for cars would likely weaken dramatically.

The reality is, the USMCA free trade status would likely hurt Detroit's Big Three – General Motors, Ford Motors and Stellantis (formerly Chrysler) – the most. It takes between 1.5 to 2 years, at a minimum, for an OEM to qualify a new supplier and move the part to production. Tariffs could grind the industry to a halt in about a week, as forecasted by Linda Hasenfratz, Chair of auto supplier, Linamar, a holding in several Sionna strategies. This would likely trigger layoffs – the majority of which would be for jobs located in the U.S.

As you can see, the ramifications are severe for U.S. consumers and manufacturers alike. A likely outcome is that the USMCA will be renegotiated earlier than the expected 2026 timeframe. While we can't say for certain what the ramifications will be for Canadian manufacturers, we have found that in the end, worst-case scenarios rarely materialize. Humans reliably avert dangers that can be foreseen.

For more on this subject, please contact us to schedule a chat with Portfolio Manager, Joanna Wolff, who covers the auto sector.

What's next?

We live in a world where the news seems to be reported at an astonishingly fast rate and is constantly changing. It's hard to ignore the noise and focus on the things that really matter, but that focus is what often helps drive good investment decisions. *The Home Country Bias Series* will parse through the noise and provide insights on several topics, and answer important questions, like:

Could the removal of carbon credits be a significant positive for Canada's energy industry?
Will the threat of tariffs cut the 'red tape' around energy projects and fast-track permits?
Will we see more economic cooperation amongst provinces?
Can the U.S. function without Canadian potash imports?
Could Canada's long-standing oligopolies in telecommunications and banking be challenged?

We look forward to sharing our thoughts with you over the coming months.

-The Sionna Team

References
**MSCI*
***Credit Suisse Global Investment Returns Yearbook 2023*
****FactSet as at December 31, 2024*

For More from Sionna on These Themes:

A Few Things we Know For Sure

A Reversion Expected

Canada Cheapest in a Decade

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