

PERSPECTIVES

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Each month, our experts decipher trends, opportunities and strategies shaping the financial universe of informed investors. Discover nuanced analysis and insights to guide your wealth management decisions. Forged by experience and driven by innovation, our perspectives help you build a sustainable financial legacy.



QUEBEC EQUITIES: LOCAL CHAMPIONS WITH A GLOBAL REACH

Who would have thought the financial markets would one day be roiled by a return to harsh protectionist policies in Washington? Yet, this is the unsettling reality of today's economic environment.

In this uncertain context, investors are increasingly aware of the relevance of supporting the growth of high-calibre local companies with robust business models. Quebec equities, which make up slightly less than 20% of the S&P/TSX Index, deserve special attention. Their unique features give them a strategic role that complements Canadian equities. Over five years, they've recorded a convincing annualized return of 14%.

Beyond preconceived ideas: understanding Quebec's investment universe

Contrary to popular perception, Quebec's publicly traded companies are not limited to the local economy. They include companies that are headquartered in Quebec (or have most of their employees or assets there) but whose influence extends well beyond the province's borders.

The universe of Quebec stocks, of which about 100 have a market capitalization exceeding \$600 billion, includes true

champions, such as WSP Global, Dollarama, CGI, National Bank and Alimentation Couche-Tard. These outstanding companies all started out in Quebec before conquering foreign markets through organic growth and strategic acquisitions. Exposure to the global economy combined with a robust business model is the key to the complementary role they can play in an equity portfolio.

The little-known advantage of sector complementarity

The sector concentration of the Canadian stock market is no secret. Financials make up about 33% of the weighting of the S&P/TSX Index, with energy and materials accounting for 30%. With this high concentration, the Canadian market is vulnerable to significant volatility caused by fluctuating commodity prices.

In contrast, the Quebec equity universe has a very different sector composition: With little exposure to cyclical sectors such as energy and materials, it is largely composed of consumer companies and industrials.

This distinctive sector allocation is a significant advantage for investors. For example, although Canadian companies reliant on raw materials can optimize their operational structures and cost efficiencies, their profitability

hinges largely on commodity price fluctuations over which they have no control. Most Quebec companies operate in the industrials and consumer products sectors; as a result, they have greater pricing power and more predictable earnings.

Companies in these sectors have one-of-a-kind, and even niche, business models, such that the value added by their management teams can truly make a difference. In-depth analysis of their strategies and business models is therefore vital.

That's why most portfolio managers agree that the Quebec stock market requires a security-selection approach.

A dual role in a global asset allocation

In addition to diversifying a portfolio, investing in Quebec equities makes it possible to support companies whose economic and social impact is local. While optimizing a portfolio's risk-return profile, this allocation also helps keep head offices in Quebec, thereby preserving essential expertise and economic vitality.

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While optimizing a portfolio's risk-return profile, this allocation also helps keep head offices in Quebec, thereby preserving essential expertise and economic vitality. In other words, investing in local champions with a global reach is a promising strategy that enhances investors' returns and supports the business ecosystem at the same time.

The proximity advantage in fundamental analysis

For a portfolio manager, geographical and cultural proximity provides a considerable advantage in the analysis of companies. It manifests itself in a variety of ways: interaction with different levels of management, facility visits, in-depth understanding of the corporate culture and so on. Such immersion provides an understanding of nuances that may escape managers based elsewhere. For example, portfolio managers with a local presence can more easily distinguish a temporary problem from a fundamental strategic issue. This ability to contextualize information becomes a significant advantage in decision making.

The sustainability profile of Quebec equities

The Quebec equity market has an appealing sector composition for investors concerned about their portfolio's environmental footprint.

The absence of sectors such as energy and coal reduces exposure to companies dependent on fossil fuels and suits investors who want to manage risks associated with the energy transition.

In addition, although the maturity of environmental, social and governance (ESG) practices varies from one company to another, a comparative

analysis of the practices adopted by Quebec companies with those of companies in the rest of Canada shows that Quebec enjoys a significant advantage.

Outlook: resilience and opportunities

In the current environment, tariff policies have created uncertainty but have not yet had a visible impact on corporate earnings. Quebec companies often benefit from a unique positioning that reduces their vulnerability. For example, WSP has a global presence, while the Canadian National Railway Company (CN) has an irreplaceable rail network that transports essential goods.

That said, after an exceptional 2024 in terms of performance (our strategy recorded a return net of fees of more than 26%), we're seeing the pendulum swing back. Even so, the recent market downturn is creating opportunities to invest in Quebec stocks whose valuations have become attractive.

Our approach: investing with conviction for the long term

Our Quebec equity strategy has an investment horizon of three to five years. It is based on strong convictions and in-depth knowledge of companies, some of which have been in our portfolio for more than 15 years.

This stability allows us to see companies' business models evolve and to meet with management teams frequently, enhancing our understanding of industry dynamics, competitive advantages and value-creation drivers.

We use a bottom-up process that favours individual stock selection and focuses on fundamental analysis to generate returns that outperform benchmarks over full economic cycles. We analyze a company's business

model before its valuation, ensuring we invest in quality companies at reasonable prices. Because Eterna's investment team is in Quebec, we're ideally positioned to understand the development of local companies and manage a portfolio that leverages local champions.

Our portfolio typically comprises about 35 stocks selected according to specific criteria, including growth potential, entry barriers, management calibre and outlook for margin expansion. Even though the portfolio is relatively concentrated, it is conservatively diversified and has a lower level of risk than the S&P/TSX Index.

This approach has allowed us to outperform the Canadian equity index in 12 of the past 15 years and achieve a net return of more than 26% in 2024. The sector complementarity of Quebec's equity market, including its reduced exposure to natural resources and energy, combined with our fundamental approach, contributes to the portfolio's resilience while supporting companies headquartered in Quebec.

Eterna's Quebec equity strategy, with more than \$200 million in assets under management, is one of the few to focus solely on Quebec companies of all sizes. It is available to institutional investors and private wealth clients.



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