

Equity team commentary: Higher for longer meets “Canada Strong”

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Key takeaways

September was a relatively quiet month on the earnings front, with Dollarama, Alimentation Couche-Tard and Descartes among the few major Canadian reporters. That earnings lull gave investors something rare: time to step back from the noise and focus on the bigger questions facing markets and determine where equities belong in portfolios in a rising risk-free-rate environment.

The TSX finished roughly 2% lower for the month, while the S&P 500 rose less than 1%. On the surface, not much happened. Underneath, however, the investment debate shifted meaningfully. Three issues dominated markets: inflation and rising bond yields, the sustainability of the AI investment cycle, and geopolitics. For Canada, there was a fourth and potentially more important question: **is the country finally prepared to capitalize on the considerable economic advantages it has and supply more of what the world increasingly needs?**

Higher for longer is back

The month opened with escalating Middle East tensions causing Brent crude to briefly approach US\$110 per barrel, reigniting inflation concerns. The Federal Reserve subsequently raised the fed funds target range by 25 basis points to 3.75% – 4.00%, its first hike since 2023.

More important than the move itself was the message: the fight against inflation is not over. Bond yields responded accordingly. The US 10-year Treasury yield moved above 5%, while the 30-year reached levels not seen in more than two decades. The term premium, or the additional yield investors demand for holding longer-dated bonds rather than rolling shorter-term securities, has re-emerged as investors demand compensation for inflation as well as fiscal and duration risk. This matters for equities because monetary policy is only a blunt tool against inflation.

Higher rates can weaken demand, but they cannot create another barrel of oil or reopen a disrupted supply chain. The consumer is already stretched, particularly at the lower end of the income spectrum, where housing, food, transportation and financing costs are absorbing a greater share of disposable income. At the same time, input pressures are appearing in areas such as trucking, copper and diesel (potentially exacerbated by President Trump's threat of a diesel export ban). That creates an uncomfortable combination for companies: softer demand on one side and persistent cost pressure on the other.

The more important development, however, is at the long end of the bond market. When investors can earn roughly 5% in a relatively low-risk government security, equities face a more credible alternative than they have had for much of the past decade. The hurdle rate for owning stocks has risen.

With that said, the market's resilience remains notable. Despite higher yields and geopolitical uncertainty, the S&P 500 has remained near record levels. But breadth has been less impressive, with an increasing number of companies trading well below their peaks. The distinction between companies generating genuine earnings growth and those that benefited primarily from lower discount rates is becoming increasingly important.

That is a constructive environment for fundamental investors. When the risk-free rate was falling, multiple expansion could mask mediocre fundamentals. At 5%, investors have considerably less reason to pay elevated prices for growth.

That dichotomy does not necessarily mean equities are unattractive. It means **price matters more**.

AI: From capex to productivity

The AI debate is also becoming more nuanced. The question is no longer whether AI will change the economy. It is whether the extraordinary pace of AI-related capital spending can ultimately translate into an equally extraordinary increase in productivity and earnings. A large portion of recent US earnings growth has been linked, directly or indirectly, to the AI investment cycle.

The critical question is what happens when the rate of spending eventually slows. If AI capex simply decelerates, the market will have to absorb a meaningful reduction in incremental demand. If, instead, productivity gains begin to replace the capex impulse through lower labour requirements, better software development, more efficient logistics and new business models, the economic payoff could be considerably larger.

The handoff, however, will not be seamless. The progression from greater computing power to more capable models to measurable corporate productivity will almost certainly be uneven. The market has increasingly priced in a relatively smooth trajectory; reality is unlikely to be that linear. The emergence of agentic AI is particularly vital right now. With the release of Meta's personal AI agent tool, Muse, we are witnessing the evolution beyond answering questions toward executing tasks and fulfilling transactions. That could make the next phase of AI adoption economically more consequential than simply producing another generation of larger language models.

"Canada Strong": From commitments to capital

For Canadian investors, the most important event of the month was arguably not an earnings report but the first Canada Investment Summit. The guest list itself was notable: global institutional investors, sovereign wealth funds, pension plans and major asset managers representing more than \$100 trillion of capital. The Summit generated nearly \$500 billion of announced investment commitments, including nearly \$100 billion from Canadian institutional investors and almost \$325 billion of new financing commitments from Canadian banks. A commitment, however, is not capital deployed.

The real test is whether projects get approved, financed and built. That means permitting, infrastructure, access to capital and attractive after-tax returns will matter far more than the headlines surrounding any individual announcement. This is where the Canada Strong thesis becomes interesting from an equity perspective.

Canada has many of the ingredients the world increasingly needs: energy, critical minerals, electricity, infrastructure, food, secure supply chains, digital infrastructure and, increasingly, defence capacity. The opportunity is not simply to own those resources. It is to **build the infrastructure required to monetize them**. That distinction matters: If Canada can move from announcing projects to actually constructing them, the economic benefits should extend well beyond the resource producers themselves. Capital spending creates demand for engineering, construction, equipment, transportation, financial services and energy. Successful projects create long-duration cash flows and, ultimately, a larger earnings pool for Canadian public companies.

The Summit's Productivity Mega Deduction is an important part of this equation. The policy expands immediate expensing to a much broader range of assets, including mining property, pipelines, fibre, software, R&D, rail, bridges and roads. Ottawa estimates the changes will reduce Canada's marginal effective tax rate on new business investment from roughly 13% to 6.4%.

The investment implication is straightforward: lower after-tax capital costs can improve project economics, increase expected returns and shorten payback periods. Combined with efforts to accelerate permitting and approvals to a one year timeframe, this represents a meaningful change in the incentive to invest in Canada. But the proof will ultimately be in the spending.

From policy to projects

Two of the clearest signposts came at the end of the month. LNG Canada and its partners approved Phase 2 of the Kitimat LNG project, a roughly C\$33 billion expansion that will add two trains and double capacity from 14 million tonnes per annum to 28 million tonnes, and the Federal Government deemed the 1 million barrel per day Pacific Link oil pipeline a project of national interest. There are precisely the kinds of developments that can turn the Canada Strong plan from an economic narrative into an investment thesis. They create additional demand for Canadian oil and natural gas, expands export infrastructure and reinforces Canada's ability to reach global markets beyond the United States. For example, TC Energy's Coastal GasLink infrastructure will benefit from the expansion, demonstrating the broader economic multiplier associated with major resource projects.

Enbridge's US\$2.55 billion acquisition of Blackstone's Tallgrass crude transportation business expands its footprint in the US Rockies and adds strategically located pipeline, storage and terminal assets. The transaction is another example of a Canadian infrastructure company using its balance sheet to consolidate long-duration, cash-generating North American assets.

The nuclear opportunity is also becoming more tangible. Cameco and Brookfield's Westinghouse announced a confidential submission of a draft Form S-1 for a proposed Initial Public Offering (IPO). While the valuation floated could exceed \$50 billion USD, it does remain subject to market conditions. The potential transaction highlights the growing strategic importance of nuclear power as electricity demand rises from AI data centres, industrial electrification and grid investment.

The common thread is important: **capital is beginning to move toward assets that Canada is particularly well positioned to supply.**

Other notable Canadian equity developments

Teck's proposed combination with Anglo American would create a globally scaled, Canadian-headquartered but United Kingdom incorporated critical-minerals company. The transaction raised an important issue for Canadian investors: whether a company with strong Canadian economic ties but a foreign incorporation or domicile should remain eligible for Canadian benchmark indices.

S&P Dow Jones Indices announced changes to the eligibility criteria for S&P/TSX Canadian indices that could allow foreign issuers with a material and substantive connection to Canada to qualify. The change is particularly relevant to the proposed Anglo Teck combination and is expected to take effect in December, potentially leading to increased index demand for the miner. For Canadian investors, this is more than an index technicality. Keeping Canadian champions in Canadian benchmarks helps preserve their representation in the domestic investment ecosystem and reduces a structural disadvantage for companies that are increasingly global in their operations and ownership.

Brookfield's Investor Days reinforced many of the same structural themes the company has emphasized for years: digitalization, decarbonization and deglobalization. Its long-term earnings ambitions remain significant. Specifically, Brookfield laid out plans to double earnings over the next five years, with growth expected to come from Wealth Solutions, Asset Management, capital deployment and realizations.

GFL also attracted attention after reports that competing infrastructure groups including a consortium involving KKR, Energy Capital Partners and Blackstone and another involving Brookfield and IFM, were exploring potential take-private transactions. Nothing substantive has yet emerged, but the interest itself is noteworthy. It illustrates the willingness of global infrastructure capital to pursue Canadian-originated assets with durable cash flows.

Finally, in a surprise move, Panama's interministerial commission recommended an "orderly closure" of First Quantum's marquee mine, Cobre Panama. The situation is still highly fluid and not finalized, but the initial reaction to the Canadian miner was swift and harsh, with the stock dropping over 30% shortly after the announcement hit the tape before partially bouncing back as additional news came out.

Bottom line

September began with three worries: geopolitics, rising bond yields and technology valuations, and ended with a more nuanced investment landscape. For US equities, the question is increasingly whether AI can transition from an enormous capital-spending cycle into an equally powerful productivity cycle, while investors contend with a roughly 5% risk-free rate and a Federal Reserve that remains focused on inflation. The implication is straightforward: investors can no longer ignore the price they are paying for growth. Quality of earnings and free cash flow matter too.

Canada faces a slightly different opportunity. The country has many of the resources and capabilities the world increasingly needs. The Canada Investment Summit, the Productivity Mega Deduction, LNG expansion and the growing flow of institutional and infrastructure capital all point toward a potentially more investment-intensive Canadian economy. But potential is not earnings. The investment opportunity comes if Canada can turn its advantages into productive assets: energy exports, mines, electricity generation and transmission, data centres, nuclear capacity, infrastructure and defence businesses. If those projects are built and generate attractive returns, the opportunity for Canadian equities could be considerably larger than the market is currently discounting.

The next phase of the Canada Strong story isn't about talking about our advantages.

It's about building them.

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