

# Future-proofing Canadian endowments & foundations: Investment strategies for sustainable growth



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Financial markets are characterized by inherent volatility and cyclical patterns that can significantly impact charitable organizations' strategies for managing their investment portfolios. Regulatory changes, such as the increase in the disbursement quota for registered charities in Canada from 3.5% to 5.0%, create additional layers of complexity for long-term financial planning. As we have witnessed many times, market dynamics are frequently influenced by policy changes and geopolitical developments – as demonstrated by the April 2025 “Liberation Day” tariff announcement – that can trigger sharp corrections followed by extended rallies. These cycles often feature concentrated gains in specific sectors or asset classes, which may mask broader economic vulnerabilities and stoke concerns about market performance sustainability due to narrow participation. For charitable organizations, understanding these recurring patterns of volatility, sector rotation, and policy-driven market movements is important for developing resilient investment strategies that can meet their financial obligations and long-term mission objectives.

This paper concerns itself specifically with endowments & foundations (E&Fs) and the unique challenges they face in volatile market environments. While short-term market fluctuations are inevitable, they intensify governance challenges, requiring stronger risk management and clearer communication from boards and investment committees.

E&Fs must anchor their investment strategies in clearly defined philanthropic goals, translating specific mission objectives – such as educational scholarships, health care initiatives, or community development programs – into quantifiable funding requirements. This strategic foundation will help determine the true required return, which must account for the 5% disbursement quota, inflation, and expenses – often necessitating ambitious return targets in the realm of 6–8%. A disciplined, long-term approach is essential for navigating volatility while maintaining predictable income streams, capital preservation, and intergenerational equity.

We have been helping E&F clients navigate the aforementioned challenges across different market environments for over forty years. This paper addresses four key areas where E&Fs can strengthen their approach to navigate this environment effectively:

- **Strategic asset allocation:** Adapting portfolio construction to balance risk, return, and liquidity needs.
- **Active management:** Understanding its value for institutions like E&Fs that must balance current spending obligations with long-term capital preservation.
- **Liquidity management:** Structuring the portfolio's asset mix appropriately to maintain sufficient portfolio flexibility for cash requirements.
- **Benchmarking and stakeholder communication:** Establishing appropriate performance metrics and transparent reporting to maintain stakeholder confidence.

## Strategic asset allocation

Establishing the investment policy asset mix is a key component of strategic decision making. This asset mix typically represents long-term target exposures to different asset classes expected to support investment objectives. For an E&F, objectives would likely involve managing short-term market volatility, sustainable growth, preserving capital, and meeting annual spending requirements.

The ability to build an asset mix that will achieve an E&F's objectives depends partly on the diversity of the opportunity set. Investment components can vary significantly based on investor preferences and classification approaches. Below is a comprehensive breakdown of the potential asset mix exposures, broadly categorized according to their role in a portfolio.

Asset mix broad exposure	Role	Rationale
Investment grade fixed income	Income, stability, capital preservation	Reliable income generator that provides liquidity and capital stability
Sub-investment grade fixed income	Income, growth	A source of higher income with capital appreciation potential
Developed market (large-cap) equities	Growth	The primary driver of long-term growth potential in a portfolio of assets
Developed market (mid-cap/small-cap) equities	Growth	A source of higher return potential that can complement large-cap equities
Emerging market equities	Growth	An alternate source of long-term growth potential driven by different economic and policy dynamics than developed market equities
Low volatility equities	Growth, downside protection	Exposure to the equity risk premium with lower volatility and downside risk
Private market alternatives	Diversification, growth	A source of diversification with exposure to alternative risk premiums and return drivers
Liquid alternatives	Diversification, stability	A source of diversification that can dampen total portfolio risk while contributing positively to returns

With the opportunity set defined, it is possible to construct portfolios that have different risk/return trade-offs and vary in terms of their complexity, liquidity, and fee profiles. The most suitable portfolio for an institution will ultimately depend on its specific beliefs, goals, and circumstances, however, all will have to consider the impact of the 5% disbursement quota. To illustrate this, we model three different portfolios:

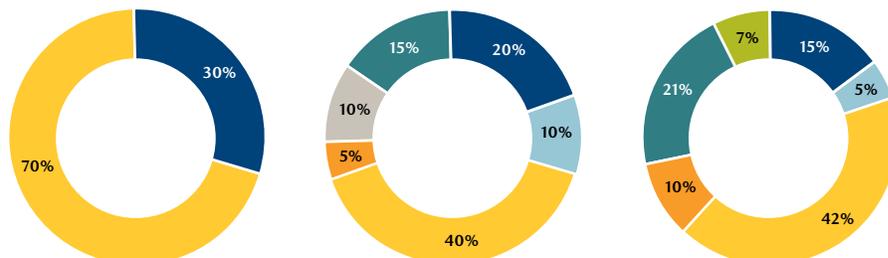
**Portfolio A:** Straightforward and fully liquid portfolio with a heavy tilt towards developed market large-cap equities.

**Portfolio B:** More diversified portfolio with a modest allocation to less liquid private market alternatives.

**Portfolio C:** More complex and illiquid portfolio with a higher allocation to alternatives as a whole.

**Figure 1: Asset allocation and risk/return metrics**

- Investment grade fixed income
- Sub-investment grade fixed income
- Developed market equities
- Emerging market equities
- Low volatility equities
- Private market alternatives
- Liquid alternatives



Modelled expectations*	Portfolio A	Portfolio B	Portfolio C
Long-term return	5.50%	6.00%	6.60%
Annual downside risk**	-17.20%	-12.60%	-12.90%
Annual volatility	10.50%	8.30%	8.30%
Sharpe ratio	0.21	0.32	0.37

\* Refer to appendix for more detailed asset class breakdowns, modelling assumptions, and disclosures.

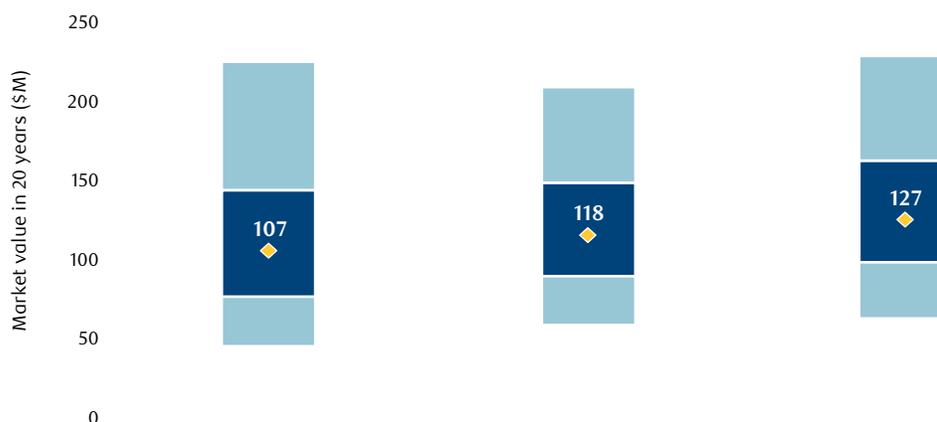
\*\* CVaR95 which represents the expected loss during the worst 5% of return outcomes. Hypothetical performance analyses are for illustrative purposes only and there is no guarantee that hypothetical returns or projections will be realized.

Figure 1 illustrates how the risk/return profile evolves as more of the opportunity set is incorporated into the asset mix. As new exposures are layered in, the expected levels of risk and return improve; however, the portfolios become increasingly complex and rely more on less liquid strategies.

While the overall risk and return statistics are valuable for understanding the trade-offs between portfolios, they do not fully capture the impact on specific E&Fs' objectives. To properly compare the effectiveness of these portfolios in

the E&F context, we examined long-term market value and spending projections that reflect the actual operation of each portfolio, including the disbursement quota. To do this, we conducted stochastic simulations using 2,000 unique return scenarios over 20 years, assuming an initial capital base of \$100 million. These projections are illustrated in Figure 2, and provide direct insights into how each portfolio preserves capital over time, supports spending needs, and achieves intergenerational equity.

**Figure 2: 20-year projections of initial \$100 million**



20-year projections	Portfolio A	Portfolio B	Portfolio C
Ending median market value (\$M)	\$107	\$118	\$127
Median cumulative amount disbursed (\$M)	\$105	\$109	\$113
Probability of preserving nominal capital	56%	68%	75%
Probability of preserving real capital	25%	27%	35%

Source: RBC GAM. Refer to appendix for modelling assumptions and disclosures. Hypothetical performance analyses are for illustrative purposes only and there is no guarantee that hypothetical returns or projections will be realized.

As we progress from Portfolio A to Portfolio C, we observe a clear improvement in key metrics. Portfolio C achieves a higher ending market value, greater total spending, and a stronger probability of preserving capital. However, the probability of preserving capital in real terms (i.e., adjusted for inflation) is notably more challenging. This reflects the impact of the higher disbursement quota, especially in today's environment. It also reflects the fact that equities are the primary driver of long-term growth potential, and we currently expect lower-than-normal future returns given highly valued and concentrated markets. This environment underscores the importance of leveraging the full opportunity set when building the policy asset mix, including greater use of specialty asset classes and alternative strategies.

### The case for active management

A further consideration for E&Fs in addressing the challenge of capital preservation is the role of active management. When expected policy returns are modest, the relative contribution of active decisions increases and can materially influence the likelihood of achieving real return targets. While this represents an important additional lever, we note that our theoretical modelling in Figure 2 is intentionally conservative and does not incorporate any potential positive impact from active management. However, in practice, it is reasonable to expect a net positive contribution from an active management strategy.

Furthermore, the magnitude of that added value is likely to increase when moving from Portfolio A to Portfolio C, given the higher allocation to asset classes with either greater overall alpha potential (e.g., emerging market equities) or where the impact of manager selection can be more significant due to higher dispersion between a top and bottom quartile fund (e.g., alternatives). This additional source of return, if realized, would increase the likelihood of E&Fs meeting their intergenerational equity goals.

In recent years, a select few mega-cap stocks have dominated market returns, leaving diversified active portfolios struggling to keep up with market benchmarks. This narrow market leadership, coupled with the rise of passive investing and heightened macroeconomic volatility, have added layers of complexity for active managers, making consistent outperformance a herculean task. Although investors have for the most part earned very healthy total returns over this period, these dynamics have naturally led them to question the value of active management.

We would argue that amidst this turmoil, active management remains especially valuable when markets turn, as skilled managers can adjust positioning and protect capital. This is an especially important consideration for E&Fs, for whom maintaining a healthy capital base is essential to support stable annual spending and safeguard intergenerational equity. Additional benefits of active management include:

- **Risk management and downside protection:** Avoiding permanent impairments during down markets is more valuable for perpetual portfolios than chasing marginal outperformance during market rallies.
- **Unlocking opportunity in inefficient markets:** Active managers can add real value, particularly in areas where information asymmetry, liquidity constraints, or limited analyst coverage create room to uncover mispriced securities.
- **Income focus:** Active managers can emphasize income resilience or credit quality, aligning directly with disbursement needs.
- **Flexibility:** The ability to pivot allocations when inflation, rates, or credit spreads shift rapidly can meaningfully contribute to performance.

Active management tends to be cyclical, not secular, meaning that its effectiveness and investor appetite fluctuate with market conditions, rather than follow a permanent trend. The current concentration in mega-cap names is reminiscent of the period leading up to the dot-com bubble in the early 2000s, illustrated on the following page in Figure 3.

**Figure 3: Historical performance of S&P 500 Index vs. active managers**



	1990-1999	2000-2010	2011-2025
Annualized return	21.57%	-2.16%	17.27%
Average median manager value add	-0.03%	2.14%	-1.31%

Source: RBC GAM, eVestment. Data from December 31, 1990 to December 31, 2025, with returns in Canadian dollars. Manager universe: eVestment U.S. Large Cap Equity universe. Number of managers in universe: between 1990-1999, active managers increased from 213-925; 2000-2010: average 1424; 2011-2025: average 1277. Past performance is no guarantee of future results.

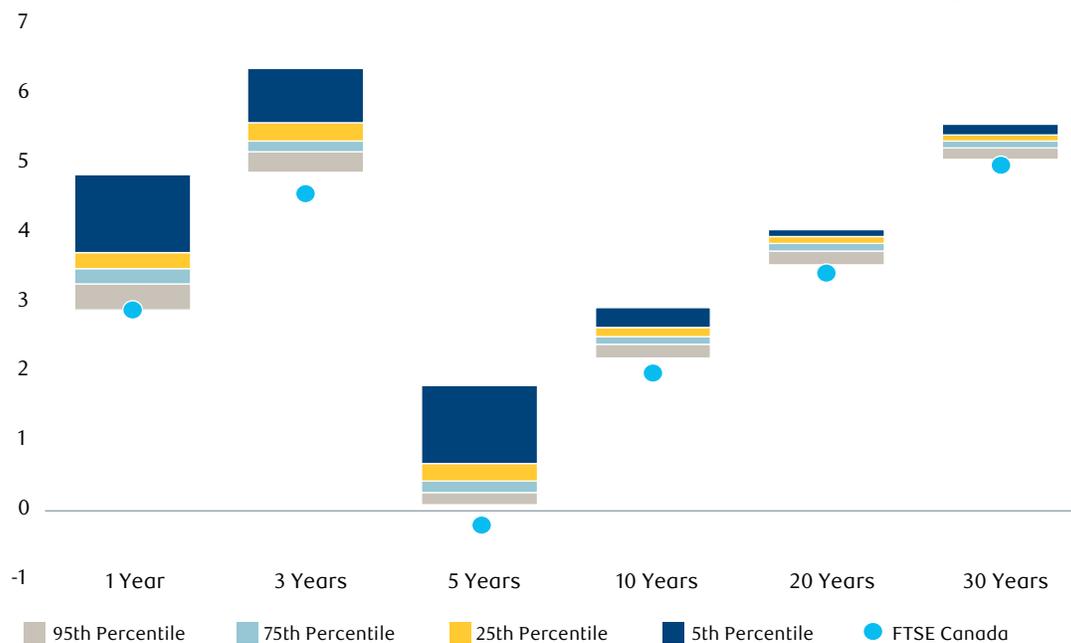
During both the 1990-1999 period that preceded the dot-com bubble as well as the latest period between 2011-2025, many active managers that were focused on risk control and valuation discipline found themselves underperforming benchmarks that were propelled by momentum and speculative enthusiasm rather than fundamentals. This dynamic created a frustrating paradox: prudent portfolio construction and diversification, long considered the hallmarks of sound investing, became performance headwinds. However, when markets suffered significant drawdowns after the dot-com bubble burst, active managers demonstrated their value proposition. As can be seen in the chart above, the median return of active managers added significant value over this period, reinforcing the merit of active management from a downside protection perspective.

From a fixed income perspective, active management offers compelling advantages that passive strategies cannot replicate, particularly given the unique characteristics of

the domestic bond market in Canada. Active managers can dynamically adjust duration, yield curve positioning, and credit exposure in response to policy shifts, economic cycles, and market volatility. Furthermore, skilled active managers can enhance returns through security selection and private placement opportunities, while providing downside protection during periods of rising rates or credit stress via tactical asset allocation and risk management techniques that passive strategies simply cannot employ.

Additionally, investors are increasingly allocating to core plus bond strategies to go beyond traditional core fixed income components while maintaining relatively conservative risk profiles. These strategies are able to invest in a broader range of sectors including high-yield corporate bonds, emerging market debt, and mortgages, for example, that can potentially deliver higher yields and better diversification. As shown in Figure 4 on the following page, active fixed income managers have historically added significant value over all time periods.

**Figure 4: Historical performance of FTSE Canada Universe Bond Index vs. active managers**



Source: RBC GAM, eVestment. Data as of December 31, 2025, based on annualized returns. Manager universe: eVestment Canadian Core Fixed Income universe. Number of managers in universe per annualized period: 1 yr: 76; 3 yr: 74; 5 yr: 70; 10 yr: 61; 20 yr: 44; 30 yr: 35. Past performance is no guarantee of future results.

Overall, active management provides the opportunity to achieve higher returns, manage risk, and maintain flexibility – all critical components for E&Fs aiming to sustainably achieve the increased disbursement quota while maintaining intergenerational equity.

**Liquidity management considerations**

All E&Fs must balance the pursuit of higher returns and diversification with the need to maintain liquidity. In recent years, many E&Fs have increased their allocations to private alternative investments such as real estate, private equity, infrastructure, and private credit in order to generate higher

returns and meet rising disbursement needs. While these investments offer attractive long-term growth potential, they also come with limited liquidity, creating challenges in managing cash flows and funding annual spending commitments, especially during times of stress.

The need for liquidity in a portfolio primarily arises from two sources: disbursements (meeting cash flow obligations) and rebalancing (maintaining investment policy limits and executing tactical adjustments). The extent to which these liquidity needs must be addressed depends on several factors that either increase or reduce the demand for liquid assets.

	Increases liquidity needs	Reduces liquidity needs
Cash outflows	Substantial lump-sum withdrawals or unexpected outflows	Predictable cash flows that represent a small proportion of the asset base
Cash inflows	N/A	Anticipated capital grants or donations
Investment income (coupons, dividends, and distributions)	Low	High
SIPP* guidelines	Rigid	Greater flexibility

\*Statement of Investment Policy and Procedures

The illiquid nature of private alternatives has created significant cashflow management challenges, particularly during the 2022 market downturn, when simultaneous declines in bonds and equities caused many portfolios to breach their Investment Policy Statement constraints due to the inability to rebalance these illiquid assets. Specific challenges that were brought on during this period and remain a concern for private market asset classes include the following:

- Private equity has been especially problematic, as exit markets remain weak and distributions continue to underperform both historical levels and investor expectations, preventing investors from accessing committed capital when most needed.
- Real estate has become increasingly inaccessible, with transaction volumes slowing dramatically and funds implementing gates that prevent investors from redeeming their holdings, effectively trapping capital during periods of market stress.
- Infrastructure investments have revealed unexpected liquidity traps, as exemplified by Thames Water’s collapse, where investors found themselves locked into a deteriorating asset with no exit mechanism, demonstrating how “stable” infrastructure can become entirely illiquid.

To effectively manage illiquidity, E&Fs should consider the following strategies:

- **Stress-test for liquidity droughts:** Assume two years of delayed distributions and assess the ability to still meet spending requirements.
- **Size allocations appropriately:** Private alternatives should not exceed what the organization can fund without jeopardizing annual distributions.
- **Assess fund characteristics:** Evaluate and categorize the level of illiquidity of strategies by manager and asset class (e.g., quarterly redemption without penalty versus vehicles with multi-year lockups for committed capital).
- **Diversify across vintage years:** Stagger commitments across multiple years to smooth distribution flows.
- **Strategy vehicle considerations:** Consider suitability of closed-end vs. open-end/evergreen funds.
- **Layer liquidity buffers:** Retain a mix of cash, short-term fixed income, or liquid alternatives, to address the unpredictable timing of capital calls, which invariably seem to arrive during market stress, when liquidity is most constrained.

To ensure that an E&F investment portfolio’s liquidity profile remains aligned with both short-term obligations and long-term investment objectives, its tolerance for liquidity events should be explicitly recognized in the investment strategy. By carefully managing illiquidity, E&Fs can optimize their portfolios to achieve their financial goals while maintaining the necessary flexibility to respond to changing market conditions and funding needs.

### Benchmarking and stakeholder communication

Meeting a higher disbursement quota can sometimes be challenging, for a variety of reasons: it could be due to periods of poor performance stemming from broad market conditions that fiduciaries cannot control, and/or sub-optimal investment decisions. This reinforces the need for a clear framework to evaluate whether an E&F’s investment processes – both in terms of asset mix decisions and fund implementation decisions – are appropriate and effective. Well-defined benchmarking and transparent communication will help stakeholders understand where performance comes from, who is accountable, and whether it aligns with long-term risk/return objectives.

Evaluating asset mix decisions can benefit from adopting clear, outcome-oriented benchmarks that align with actual spending and growth objectives. A secondary benchmark such as CPI+ (e.g., CPI+5%) serves as a more meaningful performance measure, as it directly reflects the organization’s main objective: maintaining purchasing power while funding operations in perpetuity. This approach shifts the focus from relative performance against artificial constructs to absolute performance against the organization’s actual financial requirements, providing clear accountability for investment success and more intuitive communication to boards and stakeholders about whether the investment strategy is fulfilling its purpose.

Alternatively, organizations can consider the use of a reference portfolio. A reference portfolio represents a simple and low-cost mix of public assets – typically equities and bonds (for example, Portfolio A in Figure 2 could constitute a reference portfolio for Portfolios B and C) – that is aligned with long-term return objectives and risk tolerance. Comparing the actual policy asset mix to this baseline helps determine whether additional layers of complexity and cost, such as adding specialized strategies or private assets, are contributing positively to outcomes. This framework is particularly relevant when individual asset classes appear to underperform in isolation.<sup>1</sup>

<sup>1</sup>To learn more about reference portfolios and the importance of asset mix and fund implementation decisions, please see our 2025 publication, [A new perspective on the importance of different investment decisions](#).

Fund implementation decisions also warrant careful evaluation. However, performance should be evaluated in the context of each manager's mandate. Short-term underperformance can occur for legitimate reasons. For example, during speculative market rallies, a disciplined active manager may avoid concentrated pockets of risk that drive index performance. This can produce temporary benchmark-relative shortfalls but should not necessarily reflect poorly on a manager who is adhering to the mandate's risk constraints. Furthermore, meaningful evaluation requires comparing managers against benchmarks that reflect their actual mandate and exposures. For instance, value managers should be evaluated against value-oriented benchmarks rather than broad growth-dominated indices.

When total performance is assessed relative to benchmarks that genuinely reflect the investment process, it reduces the risk of misattributing results, makes it easier to explain both successes and shortcomings, and supports more informed conversations that can lead to better decision making.

## Conclusion

A challenging market environment combined with regulatory change have presented a meaningful shift in the investment landscape for E&Fs. While challenging, this change creates an opportunity to build more robust investment frameworks.

Organizations that adapt thoughtfully – through diversified asset allocation, selective use of active management, careful liquidity planning, and thoughtful benchmarking – are likely to navigate this environment more successfully than those relying solely on traditional approaches. The current market concentration and high valuations make these areas of focus particularly relevant, as diversification and risk management become increasingly important for meeting both annual spending requirements and long-term capital preservation goals.

Success will depend on matching investment complexity to organizational capacity, maintaining clear communication with stakeholders, and focusing on strategies that align with specific mission objectives. By embracing a total-portfolio, mission-driven approach, E&Fs can adapt to this new environment and continue fulfilling their mandates not only today, but for generations to come.

# Appendix

## Portfolio asset mix allocations

	Portfolio A	Portfolio B	Portfolio C
Investment grade fixed income	30%	20%	15%
Core plus bonds	30%	0%	0%
Short core plus bonds	0%	20%	15%
Sub-investment grade fixed income	0%	10%	5%
Global multi-asset credit	0%	10%	5%
Developed market (large cap) equities	70%	40%	42%
Canadian equities	25%	15%	15%
Global equities	45%	25%	27%
Emerging market equities	0%	5%	10%
Low volatility equities	0%	10%	0%
Canadian low volatility equities	0%	10%	0%
Private market alternatives	0%	15%	21%
Commercial mortgages	0%	5%	7%
Canadian core real estate	0%	5%	7%
Global infrastructure	0%	5%	7%
Liquid alternatives	0%	0%	7%
Multi-strategy absolute return	0%	0%	7%

## Capital market assumptions (Q4 2025)

The capital market assumptions and data sources used in the modelling analysis are presented below

Asset classes	Representative data series	Expected long-term return	Expected annual volatility	Expected annual downside risk
Core plus bonds	Custom index <sup>1</sup>	4.20%	5.10%	-7.40%
Short core plus bonds	Custom index <sup>2</sup>	3.90%	2.50%	-1.70%
Global multi-asset credit	Custom index <sup>3</sup>	6.20%	8.10%	-16.10%
Canadian equities	S&P/TSX Composite Index	6.30%	16.90%	-25.30%
Canadian low volatility equities	RBC QUBE Low Volatility Canadian Equity Strategy	5.70%	12.80%	-14.70%
Global equities	MSCI World Index (CAD)	5.20%	14.20%	-23.70%
Emerging market equities	MSCI Emerging Markets (EM) Index (CAD)	7.20%	20.90%	-31.70%
Commercial mortgages*	Custom index <sup>4</sup>	6.60%	3.40%	-6.10%
Canadian core real estate*	RBC Canadian Core Real Estate Strategy	6.30%	9.60%	-13.10%
Global infrastructure*	EDHEC Infra 300 Index (Local)	6.80%	11.80%	-16.90%
Multi-strategy absolute return*	Custom index <sup>5</sup>	8.20%	6.60%	-9.10%
Inflation	Canadian CPI (Non-Seasonally Adjusted)	2.00%	1.50%	0.00%

\* Expected long-term return net of fees.

<sup>1</sup>15% FTSE Canada Federal Bond Index, 20% FTSE Canada Provincial Bond Index, 40% FTSE Canada All Corporate Bond Index, 7.5% PH&N Mortgage Strategy, 3.75% ICE BofA US High Yield Master II (CAD-H), 3.75% ICE BofA Global High Yield Index (CAD-H), 5% J.P. Morgan Emerging Market Bond Index (CAD-H) and 5% PH&N Private Placement Corporate Debt Strategy.

<sup>2</sup>40% FTSE Canada Short Term Government Bond Index, 45% FTSE Canada Short Term Corporate Bond Index, 5% PH&N Mortgage Pension Trust, 3.5% ICE BofA US High Yield Master II (CAD-H), 3.5% ICE BofA Global High Yield Index (CAD-H) and 3% J.P. Morgan Emerging Market Bond Index (CAD-H).

<sup>3</sup>7.5% ICE BofA 3 Month US T-Bills (CAD-H), 35% ICE BofA Global High Yield Index (CAD-H), 11.25% J.P. Morgan Emerging Market Bond Index (CAD-H), 11.25% J.P. Morgan Corporate Emerging Markets Bond Index (CAD-H), 7.5% J.P. Morgan Government Bond Index-Emerging Markets (GBI-EM) (CAD-H), 7.5% Credit Suisse Leveraged Loan Index (CAD-H) and 20% Thomson Reuters Convertible Global Focus Index (CAD-H).

<sup>4</sup>41% PH&N Mortgage Strategy and 59% PH&N High Yield Mortgage Strategy.

<sup>5</sup>2% FTSE Canada 30 Day T-Bill Index, 5% PH&N High Yield Mortgage Strategy, 7% RBC QUBE Market Neutral World Equity Strategy (CAD), 9% BlueBay Global Sovereign Opportunities Strategy (CAD-H), 25% BlueBay Credit Alpha Long Short Strategy (CAD-H), 10% BlueBay Event-Driven Credit Strategy (CAD-H), 10% BlueBay Structured Credit Opportunities Strategy (CAD-H), 4% CISDM Equity Long/Short Index (CAD) and 28% PH&N Absolute Return Strategy.

## Correlations

	Core plus bonds	Short core plus bonds	Global multi-asset credit	Canadian equities	Canadian low volatility equities	Global equities	Emerging market equities	Commercial mortgages	Canadian core real estate	Global infrastructure	Multi-strategy absolute return	Inflation
Core plus bonds	1											
Short core plus bonds	0.9	1										
Global multi-asset credit	0.6	0.6	1									
Canadian equities	0.4	0.3	0.7	1								
Canadian low volatility equities	0.4	0.3	0.6	0.8	1							
Global equities	0.3	0.3	0.5	0.7	0.6	1						
Emerging market equities	0.4	0.4	0.7	0.6	0.5	0.6	1					
Commercial mortgages	0.7	0.7	0.2	0.1	0.2	0.2	0.1	1				
Canadian core real estate	-0.2	-0.3	-0.2	-0.1	0.0	-0.1	-0.1	-0.3	1			
Global infrastructure	0.4	0.3	0.1	0.0	0.2	0.0	0.0	0.3	0.3	1		
Multi-strategy absolute return	0.3	0.4	0.8	0.7	0.6	0.5	0.6	0.1	-0.1	-0.1	1	
Inflation	-0.1	-0.1	0.0	0.1	0.1	0.0	0.0	-0.1	0.0	-0.4	0.1	1

Capital market assumptions represent the views of PH&N Institutional for the purposes of illustrating and understanding the potential risk-reward trade-off of different portfolio decisions and are established by considering a variety of qualitative and quantitative sources of information including: different forecasting models; internal and external research; existing and implied future conditions as priced by capital markets; and internal views of our fund managers. Expected long term annualized returns are for a 10-year forecast time horizon. Volatilities, downside risk and correlations are estimated from historical data and adjusted as required to reflect future market conditions. Investors should be aware of the limitations using forward-looking assumptions in that there is absolutely no guarantee that future performance will occur according to any ex-ante expectation.

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