Investment Commentary – June 30, 2017

Empire Life Investments

Fixed Income: The benchmark Canadian ten-year government bond yield broke out of its trading range in April, with the yield declining until early June, primarily because of a lack of inflation, the fading of reflation trade and the continued hunt for yield. The end of June saw a global coordination among major central banks to bring monetary policies back to a more normal level. The Federal Reserve raised rates, and the European Central Bank (ECB) removed the easing bias on interest rates from its forward guidance. A sudden shift in the policy stance of the Bank of Canada (BOC) pushed yields higher, after the odds of the BOC raising interest rates at least once this year increased to about 95% at the end of June, from almost zero odds at the beginning of the year. The FTSE TMX Canadian Universe Bond Index gave back some early gains and finished the quarter with a return of 1.1%. The fixed-income portfolio is positioned defensively, by reducing credit exposure and keeping the overall duration slightly shorter than that of the benchmark index.

U.S. Equity: A U.S. recession is unlikely in the foreseeable future. U.S. consumer spending rebounded nicely in March and April, supported by rising income, wealth and credit. The best job prospects in 16 years have lifted consumer confidence. Monetary policies became more restrictive than at the peak of the stimulus, but they remain accommodative. The market is likely not yet at the point at which monetary policy becomes a headwind. Driven by a combination of earnings growth and multiple expansions, the S&P 500 TR Index increased by 3.1% (0.5% in Canadian dollar terms) over the quarter, with subdued market volatility. At the end of June, the VIX index, which tracks the implied volatility of the S&P 500 over the next 30 days, reached its lowest level since 1993. Lower volatility encouraged complacency, and that might lead to a risk of investors mispricing risk. Despite having strong confidence in U.S. equities' long-term outlook, we have become more cautious on short-term prospects, primarily due to uncertainties about fiscal policies and a divergence between hard and soft economic data. Market valuations also appear somewhat stretched, as U.S. equity multiples were trading at the high end of historical averages.

Canadian Equity: The Canadian economy has been robust, as evidenced by GDP data, job growth, household spending, business investment and manufacturing activities. But investor sentiment has been somewhat bearish, with a focus on the downside risks from declining commodity prices, elevated housing prices, growing consumer debt, NAFTA renegotiations and the resulting uncertainties in international trade. Canadian equities lagged other asset classes for the quarter, with a decline of 1.6% for the S&P/TSX Composite TR Index. Oil prices fell sharply from a quarterly high of US$53.40 per barrel to US$42.53 by mid-June – a 20% bear market decline – before rebounding slightly at the end of the quarter to US$46.00. We remain positive on Canadian energy, and believe oil will likely eventually recover and stabilize in the US$50–US$60 range. Recent policy initiatives to slow down an overheated housing market are beginning to have some impact. A gradual increase in interest rates is considered positive for banks and insurance companies, and will provide support for all companies that offer defined benefit retirement plans. We expect these positive developments to improve sentiment regarding the broad Canadian equity market.

International Equity: Outside North America, the international macroeconomic environment is positive. China has stabilized, Europe is recovering, and corporate earnings in Japan are rising. International equities, as represented by the MSCI EAFE Index, led the other asset classes over the quarter, with a 6.4% gain (3.6% in Canadian dollar terms). Political drama also played out in the region, first with the French presidential election and then a snap British election. The outcomes of those events seemed to calm investors. Regardless of these outcomes, the European economy appears to have stabilized to point where the ECB may begin unwinding its bond purchase program at the end of the year. Monetary policies may not be at the peak of stimulus, but they remain accommodative. While noting the improved investment conditions in international markets, we remain concerned about the uncertainty regarding Brexit negotiations, the impact of the ECB's tapering off its monetary stimulus and long-term questions about further EU integration.

Please see page 2 for full disclaimer

(Continued)

Investment Performance – June 30, 2017

Funds	1 mth	3 mths	6 mths	YTD	1 yr	2 yrs	3 yrs	5 yrs	Since Inception	Inception Date
Money Market Fund Series A	0.00%	0.00%	0.00%	0.00%	0.01%	0.04%	0.10%	0.24%	0.24%	9-Jan-12
Monthly Income Fund Series A	-1.2%	-0.4%	0.9%	0.9%	4.5%	2.8%	3.0%	5.8%	5.3%	9-Jan-12
Canadian Equity Fund Series A	-0.8%	-1.3%	0.0%	0.0%	9.8%	6.7%	5.3%	9.5%	8.2%	9-Jan-12
Dividend Growth Fund Series A	-0.8%	-0.8%	0.1%	0.1%	14.3%	7.4%	4.8%	9.5%	8.5%	9-Jan-12
Small Cap Equity Fund Series A	0.1%	-1.4%	2.9%	2.9%	9.7%	6.6%	2.1%	7.6%	4.3%	9-Jan-12
Diversified Income Portfolio Series A	-1.2%	0.5%	2.0%	2.0%	2.3%	2.3%	3.3%		3.6%	20-Jan-14
Cons. Portfolio Series A	-1.3%	0.3%	1.7%	1.7%	3.3%	2.3%	3.0%	4.9%	4.8%	9-Jan-12
Balanced Portfolio Series A	-1.3%	0.1%	1.5%	1.5%	4.7%	3.0%	3.7%	6.2%	5.8%	9-Jan-12
Mod. Growth Portfolio Series A	-1.3%	-0.2%	1.4%	1.4%	7.2%	4.3%	4.5%	7.5%	7.0%	9-Jan-12
Growth Portfolio Fund Series A	-1.3%	-0.4%	1.2%	1.2%	9.1%	5.4%	5.0%	8.8%	8.0%	9-Jan-12
Agg. Growth Portfolio Series A	-1.4%	-0.5%	1.4%	1.4%	11.7%	6.3%	5.5%	10.3%	9.2%	9-Jan-12