Empire Life Emblem Portfolios: Asset Allocation Update

Update from the Asset Allocation Oversight Team

July 12, 2016

Summary of Asset Allocation Decisions

Asset Class	Current Asset Allocation Positioning
Fixed Income	Underweight
Canadian Equity	Overweight
U.S. Equity	Overweight
International Equity	Underweight

	Neutral Allocation*				Current Target Allocation (change from prev.)			
Emblem Portfolio	Fixed Income	Canadian Equity	U.S. Equity	International Equity	Fixed Income	Canadian Equity	U.S. Equity	International Equity
Diversified Income	80.0%	10.0%	5.0%	5.0%	75.5% (-3.0%)	16.5% (+2.0%)	5.5% (+1.5%)	2.5% (-0.5%)
Conservative	65.0%	25.0%	5.0%	5.0%	63.0% (-2.5%)	26.0% (+1.0%)	8.5% (+2.0%)	2.5% (-0.5%)
Balanced	50.0%	35.0%	7.5%	7.5%	49.0% (-3.0%)	36.5% (+0.5%)	11.0% (+2.5%)	3.5%
Moderate Growth	35.0%	45.0%	10.0%	10.0%	32.0% (-4.0%)	48.0% (+2.0%)	16.0% (+2.0%)	4.0%
Growth	20.0%	60.0%	10.0%	10.0%	16.5% (-3.5%)	61.5% (+0.5%)	18.0% (+3.0%)	4.0%
Aggressive Growth	-	75.0%	12.5%	12.5%	-	69.0% (-3.0%)	25.0% (+3.0%)	6.0%

*Neutral allocation is based on the Fund's respective long-term strategic asset allocation

Rationale

Key takeaway: Tactically Increased Canadian Equity, U.S. Equity; Decreased Fixed Income (Cash)

Tactical View:

On June 23rd, British voters surprised the markets with their decision to leave the European Union. Immediately following the result, markets reacted in an unsurprising manner with equities selling off, and the usual safe havens – bonds, gold, and the U.S. dollar – rallying.

As calmer heads prevailed, supported by expectations of further central bank support, stock markets staged a strong relief rally to end the quarter and extending into the current quarter. The S&P 500[1] managed to reach a new all-time high at the time of writing.

In our view, however, Britain's vote incrementally raises the probability of another similar geopolitical risk event. It may provide justification to other countries with brewing nationalistic sentiment to move ahead with their agendas. At the moment, the fallout from Britain's vote seems to be manageable, given market reaction. The next "shoe to fall", however, may not be.

As a result, we have tactically increased target allocations to U.S. and Canadian equities, adding exposure to gold mining stocks in the latter. These additions have been funded by a reduction in cash holdings. We believe this will better position the portfolios for downside surprises, but also upside participation should equity markets grind higher.

Recent U.S. equity market performance supports our view that it is the most resilient among the developed world. It has withstood an earnings decline, stagnant overseas economic growth, a plunge in oil prices, negative interest rates in some countries, the threat of interest rate increases from the Federal Reserve and recent geopolitical turbulence. We believe U.S. equities provide the most attractive downside protection characteristics on a currency-adjusted basis.

Gold stocks rallied in the immediate aftermath of Britain's vote, but continued to rally as equities bounced back. This is perhaps explained by market expectations of further central bank stimulus pushing bonds yields lower – and a growing number into negative territory – which is positive for gold. Should another geopolitical risk event develop, we believe gold stocks will likely benefit further.

[1] Standard & Poor's 500 Index

Empire Life Investments

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