Empire Life Emblem Portfolios: Asset Allocation Update

Update from the Asset Allocation Oversight Team

January 15, 2015

Summary of Asset Allocation Decisions

Asset Class	Current Asset Allocation Positioning
Fixed Income	Neutral
Canadian Equity	Underweight
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%	79.5% (+3%)	6.5% (-2.5%)	12.0%	2.0% (-0.5%)
Conservative	65.0%	25.0%	5.0%	5.0%	64.0% (+3%)	20.0% (-2.5%)	14.0%	2.0% (-0.5%)
Balanced	50.0%	35.0%	7.5%	7.5%	50.0% (+2.5%)	27.0% (-2%)	19.5%	3.5% (-0.5%)
Moderate Growth	35.0%	45.0%	10.0%	10.0%	34.5% (+2%)	38.0% (-1%)	23.5%	4.0% (-1%)
Growth	20.0%	60.0%	10.0%	10.0%	19.5% (+3%)	49.0% (-2%)	27.5%	4.0% (-1%)
Aggressive Growth	-	75.0%	12.5%	12.5%	-	65.0%	29.0%	6.0%

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

Rationale

Key takeaway: tactically increased fixed income, decreased Canadian equity

A number of short term global economic risks have re-emerged to start 2015. As Greece approaches a January 25th election, polls indicate the anti-austerity Syriza party to be leading by a slim margin. A strong victory by the party may lead to increased risks of a Greek separation from the European Union, and potentially reigniting a European crisis. More recently, Switzerland abandoned its minimum foreign exchange rate with the euro currency. Although the immediate effect seems to be positive for Eurozone stocks and negative for Swiss stocks, the full impact may not be known for some time. Even in the U.S., select data points have signalled momentum may be slowing. December retail sales missed analyst expectations by a large margin; very surprising given the expected boost from lower gasoline prices.

Although our medium term outlook remains favourable to equities over fixed income, we believe prudence in the current environment is warranted, particularly following strong equity market performance in 2014. In our view, U.S. equities are supported by a domestic economy with relatively strong momentum, and a currency that is likely to benefit should global risk aversion increase; Eurozone stocks may benefit should the European Central Bank announce a large scale quantitative easing program; while Canadian equities offer value opportunities, but face uncertainties surrounding commodity prices, and its potential ripple effect on the Canadian economy and currency. **As a result, we have tactically widened our underweight allocation in Canadian equities, remain overweight in U.S. equities, and underweight in international equities relative to each Fund's longer term strategic asset mix**.

Declining bond yields reflect recent risks, with 10 year government bond yields at 1.56% in Canada, 1.77% in the U.S., and 0.47% in Germany (as at January 15, 2015). This equates to a yield decline of 22 bps, 35 bps, and 15 bps, respectively...in just one month*. Combine the aforementioned uncertainties with oil's downward pressure on already low inflation levels, and it is our belief bond yields will likely stay lower for longer. Additionally, recent data has pushed expectations for the first interest rate increase by the U.S. Federal Reserve from the spring of 2015 to the back half of 2015 instead. **As a result, we have tactically increased our fixed income target allocation to a neutral position relative to each Fund's longer term strategic asset mix**.

* December 15, 2014 to January 15, 2015

Empire Life Investments

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