Empire Life Investments

December 2018

Dear Clients:

As we write this commentary just before the holidays, most major global equity markets are tracking to finish 2018 down anywhere from ten to twenty percent. Across these equity markets, the majority of year-to-date declines occurred over the past three months. As an example, from September 20 to December 20, the total return for the S&P 500 was -15.4%*. We have not witnessed this type of equity market volatility since 2008 during the financial crisis.

Multiple factors have been responsible for the recent equity market weakness including US/China trade tension, central bank tightening, and the European Union crisis (Brexit and Italian fiscal deficit standoff).

In what has been a difficult finish for equity markets in 2018, there are a couple of important points we would like to highlight as we look forward to 2019.

Equity valuations globally have significantly declined. As an example, the twelve month forward price-to-earnings ratio of the MSCI World Index has declined to ~13.5x from ~17x at the end of 2017*. As a result equity markets have much more room to respond positively to good news as we move into 2019. We are certainly finding many more high quality companies at attractive valuations, some at levels we have not seen since the financial crisis!

With the rapid growth of exchange traded funds over the years there is a much larger presence of passive mandates which has placed less emphasis on equity fundamentals and valuation. This has contributed to the heightened equity market weakness over the past few months. In this environment, our bottom-up, value disciplined and long-term fundamental driven approach to investing has increasingly allowed us to deploy capital into high quality companies at compelling valuations.

It is difficult to predict political outcomes. Regardless of the economic environment it is high quality companies with strong management teams, solid competitive positioning, conservative capital structure and compelling long-term growth prospects that tend to outperform over the long run.

Equity market weakness especially over short periods is not ideal; however, we are working hard to take advantage of this volatility. Guided by Empire Life Investments' strict adherence to value and fundamentals, we are positioning the portfolios to continue to generate outsized returns as the market recovers.

Thank you for your support,

Ian Hardacre, MBA, CFA
Senior Vice-President and Chief Investment Officer
Empire Life, Chief Investment Officer, Empire Life Investments

*source: Bloomberg

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