2016 Mid-Year Economic and Market Outlook Conference Call

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The following is a summary of the views expressed by Empire Life Investments Inc. during a conference call on July 19, 2016.

The flight to safety that started in early 2016 showed no sign of reversing. Yields hit record lows around the world amid concerns about a weakening global economic outlook and financial market uncertainty prompted by the U.K.'s decision to leave the European Union ("Brexit"). Investors are warming up to Canadian stocks after what has been a challenging two-year period that saw the slump of commodity prices, an economic recession and a bear stock market in Canada. U.S. equities rallied to a record high, despite declining earnings, 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 Brexit turbulence.

Market and Economic Developments

- Bond yields were driven up and down by a violent swing in the oil prices in the first few months of the year. In May, Canadian bonds did not share the higher U.S. yields brought on by speculation about an imminent interest rate increase by the Federal Reserve. Weak Canadian economic data and the Fort McMurray wild fire damped expectations for future growth and inflation, prompting a rally in bond prices and a decline in yields. In June, the surprising British referendum result raised the expectations that global central banks would step in and work to limit the fallout. Investors bought sovereign government bonds as a safe haven. Bond yields around the world plunged to their record lows. The universe of negative-yielding global sovereign bonds has increased to almost US$12 billion at the end of June. Canadian bonds also benefited from the move. The Canadian yield curve fell and flattened for the first half of the year. Credit spreads narrowed, boosting the outperformance of the provincial and corporate bonds. High-yield bond was the best-performing sector. The FTSE TMX Canada Universe Index, the Canadian fixed- income benchmark, posted a gain of 4.05% for the first half of the year.

- The Canadian equity market rebounded in response to indications that Canadian economy has been somewhat stronger than widely expected. The adverse impact of the weaker oil price has thus far been limited mainly to oil-producing provinces such as Alberta. Economic growth in Quebec, Ontario and British Columbia has been solid, largely as a result of an accommodative monetary stance and expansionary fiscal policies. The fall of Canadian dollar is also stimulative. The continuation of the

U.S. recovery also helped Canadian exporters. Oil prices rallied more than 84% from the low set early in the year, stocking growth in the economy and easing pressure on energy companies and banks. The gold price benefited from a weakening U.S. dollar, the falling interest rates, and rising demand for safe-heaven assets. That helped push the Materials sector up by 52.3%. Energy surged by19.3%, and Financials advanced 5.1%. All the other sectors posted positive returns, except Health Care and Information Technology, driving the S&P/TSX Composite Index to total returns exceeding 9.8% at the end of the first half of the year.

- Fears of recession and deflation generated a negative feedback loop between oil prices and equity prices. The S&P 500 Index plummeted more than 10% in the first six weeks of the year. After that, the U.S. equity market staged a strong recovery, driven by a surge in the oil price, a continually supportive monetary policy, a pause in the U.S. dollar's long-term rally and stabilization in the Chinese economy. In June, turmoil sparked by Brexit swept across global financial markets. The U.S. equity market lost more than 5% in two days. A calmer tone prevailed following the Brexit-driven turbulence. U.S. equities regained most of the ground they lost in the two days following the U.K. referendum. Companies generating stable earnings and paying decent dividends have been bid up against the backdrop of a declining global bond yields. At the end of June, the Telecommunication Services and Utilities sectors both rose by about 25%. The Energy sector is an obvious beneficiary of the recovering oil prices. It went up by more than 16%. The S&P 500 TR Index gained 3.84% for the first half of the year. In Canadian dollar terms, however, that return becomes -2.40%, because of the appreciation of the Canadian dollar.

Outlook and Fund Positioning

- The fact that global neutral interest rates are lower than they were before the financial crisis has helped anchor bond yields at low levels. The negative-interest-rate policies of the Bank of Japan and the ECB have created a tailwind for the U.S. Treasuries and Canadian government bonds, whose yields are much higher than the negative numbers we see in Japan and on the European continent. Our base-case scenario is that the bond yields will continue to stay low for a long time. With Britain voting to exit the EU, downside risks have increased for a global economy that was already anemic. The Fed will most likely postpone a July or September rate hike. The Canadian economy is expected to contract in the second quarter as a result of Alberta's wildfires and a continuing slump in business investment. The Bank of Canada will most likely stay on the sidelines well into next year. The environment is favorable to the fixed- income market. However, with yields now being at such low or negative, bond returns derive almost entirely from price movements, meaning capital gains. Once yields unexpectedly rise and prices fall, losses could be sizeable. The bond portfolio duration is

slightly shorter than neutral, with an overweight position in corporate bonds that will mature within five years. High-yield bonds account for around 5% of assets. Corporate bond maturities are at the shorter end of the yield curve, while provincial and government bond maturities are at the longer end of the curve.

- The WTI oil price prices may be range bound between US$40 and US$60, but there are signs that oil prices appear to have reached their bottom. The impact of the drop in energy investment is expected to diminish over time. Positive developments in the Energy sector are likely to contribute to growth in the Canadian economy and ease pressure on the balance sheets of banks exposed to the sector. The Canadian equity markets are fairly valued. The stock prices are largely in line with the companies' intrinsic value. The technical signals for Canadian equity markets are fairly good. Expansionary fiscal policies and an accommodative monetary stance provide tailwinds to the Canadian economy. The direct impact of Brexit on Canada's economy and financial markets are fairly limited. Looking ahead, macroeconomic events that could have a negative impact on the Canadian economy include further oil price volatility, a weakening Chinese economy and uncertainty about the strength of the U.S. economy. The continued strong Canadian housing market also remains a risk to Canada's economy. The investment strategy will continue to focus on investment in high-quality companies that have strong balance sheets, sustainable competitive advantages, solid returns on equity, quality management teams and what the manager believes to be reasonable valuations.

- The U.S. equities' latest all-time high has come more than a year after the previous peak in May 2015. The rally supports our view that it is the most resilient market in the developed world. We believe U.S. equities provide the most attractive downside protection characteristics on a currency-adjusted basis. However, the corporate earnings are under pressure from slow global growth and, a stronger U.S. currency that has weighed on the foreign income of multinational blue-chip companies. The crash of oil prices has weighed heavily on the earnings in the Energy sector. Overall, the performance of corporate earnings has been uninspiring. However, there are tentative signs that the earnings are about to bottom. Trading at around 17 times of the forward earnings, the S&P 500 Index is fairly valued. For the market to advance notably beyond this point, corporate earnings must grow in order to justify more gains in stock prices. The current environment is prone to heightened volatility. The manager has added some defensive names in the tobacco and beverage industry in an effort to balance risks. The Financials sector presents some value opportunities. The market's next leg up will most likely to have contributions from that sector.