



Economic Outlook

Overall Theme: Fiscal and Monetary Stimulus – short and long-term impacts

- While the credit crisis has dragged down the global economy, aggressive government response provides the grounds for an improvement in the economy later in the year. Most major economies have rolled out fiscal and monetary stimulus on a scale and breadth never seen before. Central banks of the major economies have radically cut interest rates and most are now deploying unconventional measures to restart and stimulate credit markets.
- The impact of the stimulus will eventually find its way into the economy and help support it in its recovery. The measurable impacts of these actions might be delayed as this stimulus money will take time to flow to the parts of the economy where it is most needed. However, the sheer size of the stimulus is bound to have a positive impact on economic activity.
- The unfortunate long-term aftermath consequences of these actions are likely to be inflationary. While short-term forces tend to be more deflationary in certain parts of the economy, we will remain vigilant regarding the eventual impact of the stimulus actions as we position our portfolios with a long-term view.

U.S. Economy: Stimulus money to provide the necessary spark to a long recovery

- Stimulus measures and other aggressive policy responses to unclog credit markets and enhance liquidity should eventually help stabilize the economy and improve the earnings outlook.
- Abnormal credit conditions are exacerbating the pain that naturally comes with economic slowdowns. The authorities have recognized this vital issue and have enacted programs to help remove toxic assets from the balance sheets of the country's financial institutions. Significant impacts are likely to lag but the program is viewed as a very significant step in the right direction towards a return to more normal credit markets.
- Problems in residential real estate continue as the attention begins to shift towards developing issues in the commercial property market.
- Despite the reduction efforts already deployed, the magnitude of household and corporate debt outstanding remains very significant. We should anticipate the effects of deleveraging to continue for some time as the U.S. economy continues to purge itself of the excesses of the past decade. This deleveraging will impose a drag on consumption and investments in the United States, thus dampening economic, employment and earnings growth for some time.

Canadian Economy: Sound foundation but not immune to the global crisis

- While Canada is not as affected as some other economies, the global credit crisis had an impact during the first quarter of 2009.
- Reductions in exports to the U.S., as a result of the plunge in demand with our main trading partner, are largely to blame for the decline in GDP again this past quarter.
- The Canadian manufacturing sector, which exports about half of its total production, continues to struggle, along with the construction sector. In fact, in March, 85% of total job losses in the country originated from these two sectors. Since the start of the recession, around two thirds of total job losses have occurred in Ontario and British Columbia.
- We anticipate the economic situation at home to remain strained for some time but firmly believe that Canada, in part due to its sound banking system, is in better position than many other economies to weather the storm.



investment commentary



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Market Outlook

Equity Markets: More bumps on the road to recovery

- We anticipate a long road ahead while the underlying problems in financial markets and the impacts of these on corporations and consumers are being resolved.
- It appears that in March a greater risk appetite returned to the markets. However, the economic and financial backdrop remains uncertain and any further deterioration in economic data, disappointing corporate earnings, or fresh shocks from the financial sector could derail a bear market rally. We still remain cautious against taking an aggressive stance towards equity markets in general.

Fixed Income: Attractive yields in corporate bonds

- Corporate credit spreads remain elevated while at the same time, the massive flight-to-safety resulting from the financial crisis has placed downward pressure on government bond yields. Very recently, spreads have begun to narrow showing initial signs of a return of confidence in the financial system. Evidence of a sustainable economic recovery must be present before corporate credit spreads narrow significantly further.
- The mid to long-term aftermath impacts of the massive amount of stimulus money are likely to be inflationary.
- The combination of inflationary pressures and the reversal of the flight-to-safety trade point to eventual higher long-term government bond yields.
- The corporate bond segment, with its attractive yields and wide spreads, in combination with shorter duration present better protection against the impact of higher rates in the fixed income markets than would result from longer dated government bonds.

Portfolio Positioning

- General investment focus is placed on balance sheet strength, earnings visibility and consistent income generation.
- With a view towards a return of inflationary pressures following the deleveraging process, and in keeping with the mandate of each Fund, investments in resources are favoured as a general theme. These include investments in Energy, Materials and other assets that outperform under inflationary conditions.
- In our fixed income portfolios, the positioning is driven by three main factors; (1) a substantial reversal of the flight-to-safety trade away from government securities, (2) an eventual return of inflationary pressures, and (3) the compelling values found at present in high quality corporate bonds. Our fixed income portfolios maintain a duration lower than that of the market and have significant overweight positions in good quality corporate bonds.



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