

# EMPIRE LIFE DIVIDEND GROWTH FUND UPDATE

August 8, 2022



**DOUG COOPER, CFA**  
Senior Portfolio Manager,  
Canadian Equities

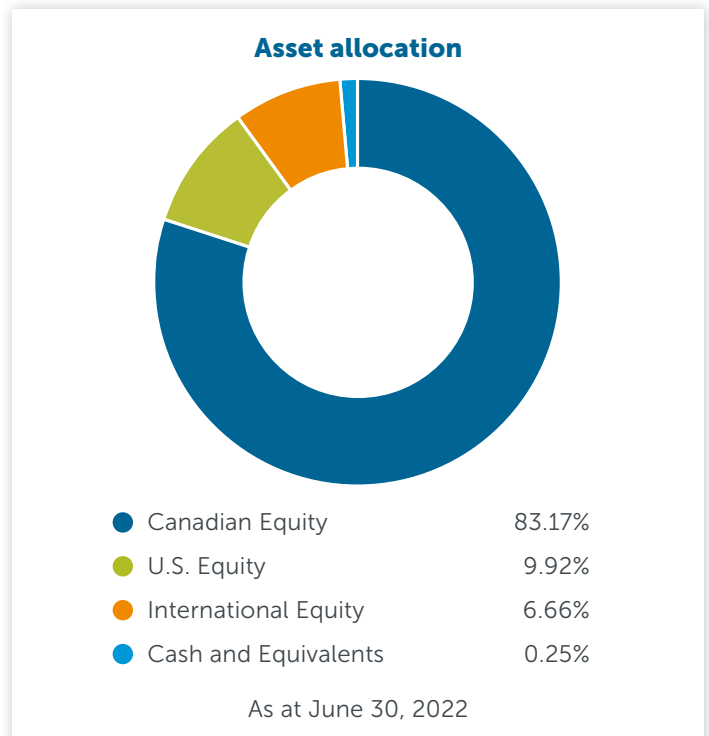
## Empire Life Dividend Growth fund outperforms in a declining market year to date

So far this year equity markets have been extremely volatile. Over this time period, the Empire Life Dividend Growth fund has behaved as expected outperforming a material decline in Canadian equity markets and an even steeper decline in equity markets globally.

As an example, the Empire Life Dividend Growth fund returned -8.7% compared to a return of -9.8% for the S&P/TSX Composite Index, a 20% decline for the S&P 500 and an 18.4% decline for the MSCI World Ex-US Index as of June 30, 2022.

Relative to the S&P/TSX Composite Index, the fund's underweight in technology was a major contributor to its outperformance. The technology sector was down over 50% during the year-to-date period primarily driven by Shopify's stock which declined by nearly 80% over the same time period. The fund's overweight position in consumer staples was also a major contributor to its outperformance.

Insurance & Investments  
Simple. Fast. Easy.®



## Russia/Ukraine conflict continues to create economic instability in the region

The fund's allocation to international and U.S. equities detracted from performance relative to the S&P/TSX Composite Index. The underperformance of international equities is mostly attributable to the Russia/Ukraine conflict which due to Europe's proximity to the conflict and reliance on Russia's energy has created substantial economic headwinds for the region. The fund reduced its exposure to international equities shortly after the start of the conflict and allocated the proceeds into Canadian equities seeing better opportunities in this asset class. Today, international equities make up ~7% of the portfolio compared to ~14% at the end of 2021 and Canadian equities account for ~83% of the portfolio versus ~73% at the end of 2021. U.S. equities make up ~10% of the portfolio which is down slightly compared to the end of 2021.

## Rising interest rates resulted in a notable change in market leadership

In what has been a quickly rising rate environment year-to-date, there has been a notable divergence in performance across sectors and styles. Steadily declining interest rates historically have been a real challenge for dividend mandates, especially for those focused on Canadian equities. A sharp rise in interest rates this year has resulted in a notable change in market leadership. High valuation and high growth companies, in particular technology companies, have underperformed materially. This was an additional factor behind the outperformance of Canadian equities – and in particular dividend mandates – during the year-to-date period especially relative to US equity markets that have significantly more exposure to growth stocks.

## The Fund's flexibility help take advantage of global opportunities

The fund's flexibility to invest outside of Canada is allowing it to take advantage of the aforementioned change in market leadership. As an example, it recently added to its Alphabet Inc. position when the stock's valuation compressed to an attractive ~16x forward earnings. While the business faces some near-term earnings uncertainty from a slowdown in advertising spend this appears to be mostly priced-in and the fund continues to have a favourable view of the company's competitive positioning and longer-term growth prospects.

## The Fund maintains a conservative exposure to energy

Prices of most commodities have experienced a material sell-off over the past two months due to concerns surrounding slowing global economic growth caused by a few factors including:

1. Aggressive monetary tightening by central banks to control runaway inflation
2. Headwinds facing consumers and businesses globally from higher inflation, particularly in Europe
3. Slowing growth in China caused by the country's zero COVID policy.

The vast majority of the fund's commodity exposure consists of oil and indirect exposure to natural gas via mid-stream energy companies. While oil prices have declined by nearly 30% over the past two months, WTI oil prices are still up nearly 20% year-to-date and at nearly \$90 continues to allow the fund's producers – including Canadian Natural Resources Inc. and Suncor Energy Inc. – to generate substantial free cash flow. Producers make up less than a third of the fund's ~15% energy weight with the large utility-like pipelines, namely Enbridge Inc. and TC Energy Corporation, making up over half of the fund's energy exposure. Europe's shift away from Russia as a source of energy is expected to be a major beneficiary for natural gas demand in North America and would require additional infrastructure to accommodate this demand thus positioning the fund's mid-stream companies like Enbridge Inc. and TC Energy Corporation very well.

While there could be additional volatility in oil prices, supply dynamics remain favourable which should limit downside to prices barring a major contraction in economic growth. The supply challenge for oil is due to years of underinvestment in production from investors pushing for more capital discipline and renewable energy. As an example, despite the recent sharp rise in oil prices producers have remained apprehensive to put growth capital to work. More recently, the Russia/Ukraine conflict has further exacerbated supply issues with a significant portion of its oil exports no longer available to global markets.

## The Fund continues to trade around its Canadian bank exposure

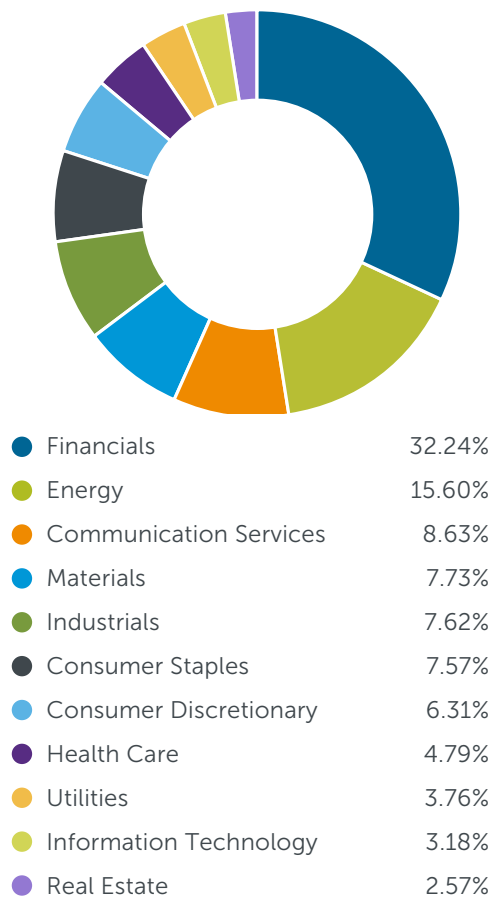
At the end of 2021, the fund selectively lowered its exposure to Canadian banks due to valuation after the stocks had run up quite materially. During the year-to-date period, the share prices of Canadian banks have come under significant pressure from concerns surrounding global economic growth and the impact of higher interest rates on the Canadian housing market. As a result, valuations have declined for the Canadian banks, but with greater uncertainty around short-term earnings the fund has yet to redeploy significant capital into the Canadian banks waiting for either a more attractive valuation and/or stabilization in the outlook for global economic growth. The fund's overall financials weight remained relatively unchanged during the period at approximately 32% with a lower weight in Canadian banks today offset by a relatively new position in Intact Financial Corporation.

## In summary

During the year-to-date period the conservative positioning of the Empire Life Dividend Growth Fund has allowed it to outperform the broader equity markets during some very volatile market conditions. Moreover, Canadian equities have outperformed global equities during the period—the fund allocated more capital to Canadian equities during the period seeing more opportunities in this asset class especially compared to international equities. While the fund's non-Canadian exposure has detracted from fund performance during the period, the high-quality nature and defensive attributes of these businesses coupled with compelling valuations position these companies to do very well over the long run.

As always, thank you for your continued support.

**Equity sector breakdown**



As at June 30, 2022

> Contact your advisor to discuss how Dividend Growth can fit into your portfolio, or visit [empire.ca](http://empire.ca) for more information.

This article includes forward-looking information that is based on the opinions and views of Empire Life Investments Inc. as of the date stated and is subject to change without notice. This information should not be considered a recommendation to buy or sell nor should it be relied upon as investment, tax or legal advice. Information contained in this report has been obtained from third party sources believed to be reliable, but accuracy cannot be guaranteed. Empire Life Investments Inc. and its affiliates do not warrant or make any representations regarding the use or the results of the information contained herein in terms of its correctness, accuracy, timeliness, reliability, or otherwise, and do not accept any responsibility for any loss or damage that results from its use.

Past performance is no guarantee of future performance.

Empire Life Investments Inc., a wholly owned-subsiary of The Empire Life Insurance Company, is the Manager of Empire Life Mutual Funds and the Portfolio Manager of Empire Life Segregated Funds. The units of the Funds are available only in those jurisdictions where they may be lawfully offered for sale and therein only by persons permitted to sell such units. Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund and segregated fund investments. **Any amount that is allocated to a Segregated Fund is invested at the risk of the contract owner and may increase or decrease in value.** A description of the key features of the individual variable insurance contract is contained in the Information Folder for the product being considered. Segregated Fund policies are issued by The Empire Life Insurance Company.

® Registered trademark of **The Empire Life Insurance Company**. Policies are issued by The Empire Life Insurance Company.

**The Empire Life Insurance Company**

259 King Street East, Kingston, ON K7L 3A8 • 1 877 548-1881 • [info@empire.ca](mailto:info@empire.ca) • [empire.ca](http://empire.ca)

**Insurance & Investments – Simple. Fast. Easy.®**

INV-3402-EN-08/22

