SUN LIFE GRANITE MANAGED PORTFOLIOS

Tactical Update

August 2021 | Opinions as August 15, 2021

The views expressed in this tactical update apply broadly to all Sun Life Granite Managed Portfolios, whereas the tactical highlights and allocation data in the chart below are specific to Sun Life Granite Balanced Portfolio. For the latest information about other Sun Life Granite Managed Portfolios, including Sun Life Granite Managed Income Portfolios, please refer to our quarterly fund reviews published at sunlifeglobalinvestments.com.

The market's 17-month bull run continued in August, with the S&P 500 setting new highs. Many of the themes that have stoked investor confidence, remain in place: interest rates are effectively at zero, more fiscal stimulus could be coming in the U.S. and earnings growth remains solid. But there are cracks starting show. Among them: the economy, hampered by the Delta virus has slowed, valuations are stretched and China's sweeping regulatory crackdown added to concerns about the country's slowing growth.

The future direction of interest rates could also trigger volatility in the weeks ahead. The U.S. Federal Reserve has continued to prioritize employment over inflation and held the line on interest rate increases. But at its August meeting, it did discuss reducing (tapering) its $120-billion-a-month, bond buying program. Following the 2008 financial crisis, the market had a "taper tantrum" and sold off when the Fed announced it was about to taper. This time the market, looking for a clear signal from the Fed, shrugged it off – at least for now.

From our perspective all these risks back into our risk/return equation. As such, we have reduced our equity exposure to neutral. However, despite the S&P 500's run-up, we still believe the U.S. market has the strongest upside.

In terms of U.S. equities, as we brought our weighting down to neutral, we continued to hold high-quality growth companies. However, we increased our exposure to value and cyclical stocks, through both active and passive strategies. And we have a sleeve of global small-and-mid-cap equities. While growth and value have led at different times in the market rebound, we believe value could lead again as the next leg of the economic recovery kicks in. Ultimately, however, we expect growth to resume its leadership.

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TACTICAL HIGHLIGHTS

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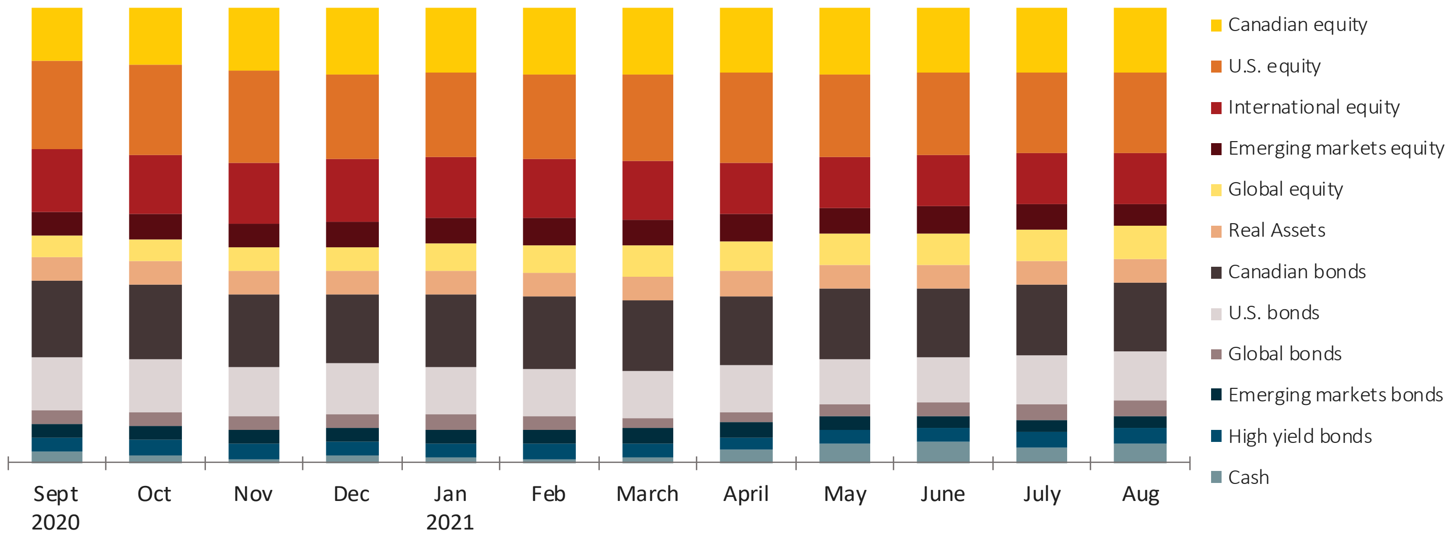
CHANGE	RATIONALE
Reduced exposure to U.S. equites	Valuations stretched after long rally
Reduced weighting in emerging market equities	Slowing growth, regulatory crackdown in China
Moved to overall neutral equity weighting	Valuations, growth and interest rate concerns

TACTICAL ALLOCATIONS | SUN LIFE GRANITE BALANCED PORTFOLIO



Allocations are as of month-end unless otherwise noted and subject to change without notice.

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Over the last year, the S&P/TSX Composite index, up 21% for the year on August 30, has been one of the top-performing markets. It has benefitted from the country's employment recovery and high vaccine rates. As well, consumer debt levels have dropped, and the savings rate has increased. The energy sector, buoyed by the doubling in the price of oil over the last year, has also helped the economy.

Valuations on the S&P/TSX are not as high as the S&P500. But after its strong run-up, we held to our neutral position in August. That said, the index is heavily weighted in energy and financials. Both of those sectors have been top performers this year. They could continue to perform well if interest rates rise and a global recovery continues to support higher oil and gas prices.

Throughout the market rally our largest equity overweight was in emerging markets (EM). But with headwinds in a number of areas, we have moved to neutral. For one, China, in what President Xi Jinping calls "common prosperity" has clamped down on a broad number of sectors. At one point, Xi's campaign erased the market value of the country's largest companies by $1 trillion.

As well, while vaccination rates have started to trend up in many EM countries, the rollout has been inconsistent and hindered economic growth in others. Moreover, the Fed is moving closer raising interest rates. This could cause the U.S. dollar to rise in value. While this would help EM countries exporting products priced in U.S. dollars, it would hurt more import dependent economies.

MSCI Emerging Markets Index was up just 2.5% for the year on August. 30. However, some major EM countries including India and Brazil have performed well. And we are being selective, both in terms of market segments and individual countries.

At minus 1.5% international equities are our largest underweight. The European economy is improving, but at slower pace than the U.S., with growth expected to come in at 4.6 % in 2021. While 70% of Europeans are now fully vaccinated, a slower rollout of vaccines compared to the U.S., led to longer lockdowns and has been a major factor in holding back the recovery. At 6% of GDP there has also been less fiscal support for the Eurozone economy, compared with 14% in the U.S. However, we will be looking for opportunities to invest in the coming months.

Canadian bonds were down 2.4%, and U.S. Treasuries 0.6% for the year at the end of August. By comparison high yield corporate bonds were up 3%. Given this, we continued to be underweight duration sensitive issues, and we expect some expansion of yields to further hurt their performance. Alternatively, we remained overweight high yield corporate bonds, with a specific allocation to intermediate-term corporates.

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