SUN LIFE GRANITE MANAGED PORTFOLIOS

Tactical Update

JULY 2022 | Opinions as of August 11, 2022

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.

Financial markets started July on a somber note after ending one of the worst first-half calendar year performances in recent memory. The effects of U.S. Fed's aggressive monetary tightening started showing up in various data. Two consecutive quarters of falling U.S. Gross Domestic Product (GDP), cooling housing markets and sinking consumer and business confidence sparked recession fears into markets.

Through mid-July, equity markets started to question the Fed's ability to hike interest rates and avoid an economic slowdown. As the 'bad news is good news' narrative took hold, market sentiment improved assuming the Fed will have to pivot to cut rates as early as the first half of 2023, pivoting from its current tight monetary stance. U.S. equities were so convinced of this view that they pulled ahead despite a 75-basis points hike during the July meeting. The S&P 500 ended July on an exuberant note rising 9.1%, its best monthly gain since November 2020. Further, a lower-than-estimated U.S. Consumer Price Index (CPI) figure of 8.5% in July gave rise to hope that inflation had peaked, and markets climbed further. Growth assets in particular rose swiftly. By early August, the Nasdaq had bounced 20% higher from its June lows. Bond markets, on the other hand, were more volatile than equity markets. Even as 10-year Treasury yields relented from 3.5% in June to 2.8% in early August, they were more sceptical about the Fed relenting its tighter monetary stance. For instance, despite a falling July CPI, the yield curve stayed inverted with the spread between 2-Year and 10-Year Treasuries falling to 58 basis points. Even the spread between 3-month and 10-year bonds turned negative briefly in August, questioning the expectation that the Fed would soon cut rates.

We believe equity markets are ahead of themselves in expecting monetary loosening from the Fed. In fact, we believe the current equity rally, which has resulted in easier financial conditions, could interfere in the Fed's fight against inflation. As expected, Fed policymakers implied they were trying to temper market enthusiasm in speeches following July's policy meeting.

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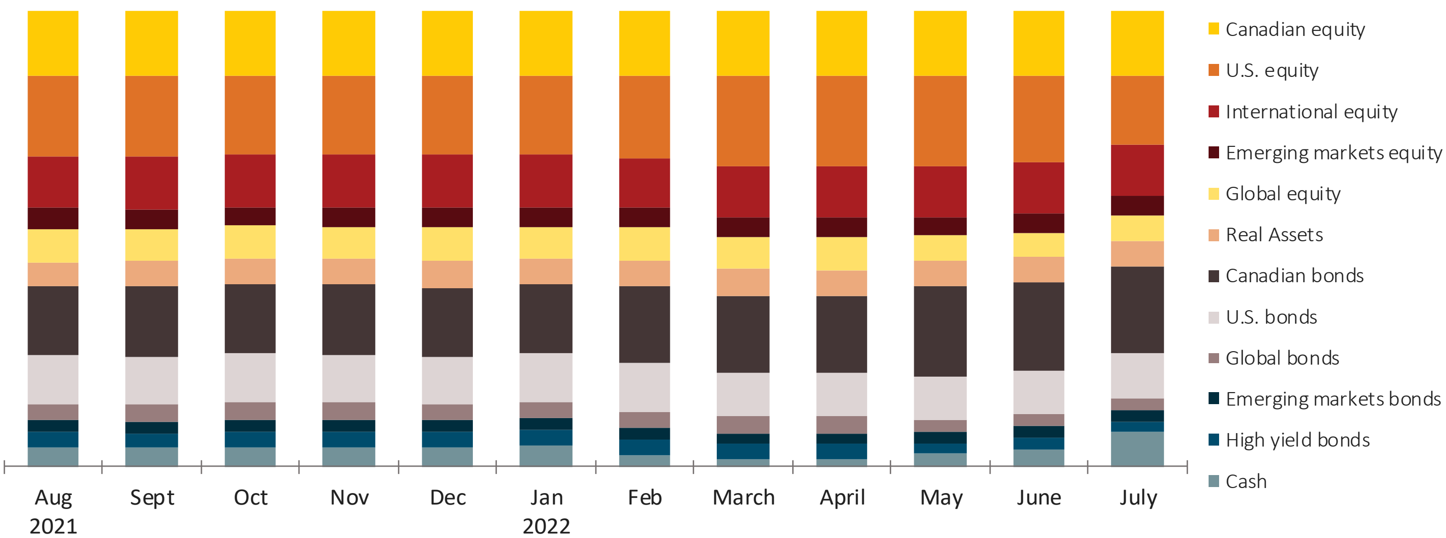
TACTICAL HIGHLIGHTS

CHANGE	RATIONALE
Underweight cyclical equities and trimmed U.S. equity exposure	Used the current market rally to derisk portfolios. We think the Fed's shift to a looser monetary policy is some way off.
Overweight cash	We expect tighter monetary policy to result in higher volatility and attractive yields.
Underweight credit	Took advantage of narrower spreads to derisk credit on the face of growth 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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While a drop in July CPI data is a positive, we expect the Fed to wait for consecutive lower inflation numbers to alter its tightening path. In addition, we are concerned about an earnings recession during slowing growth. We continued to take advantage of the equity rally to trim our exposure to U.S. equities and increased our cash exposure. Our positioning also favors defensive equities over cyclicals.

While the volatility in fixed income has presented more opportunities, we estimate yields are far from attractive. For instance, the recent strong run amongst energy issues in the high yield space has led to a compression of yields across the sector. Yields are currently hovering close to median levels seen in non-recessionary months, and we believe they are not reflective of looming economic risks. However, our outlook for Canadian core bonds is positive. We believe the housing-dominated Canadian economy is more sensitive to higher interest rates amidst record levels of consumer and mortgage debt. Any pause in Canadian rate hikes could benefit high quality core fixed income, and we maintained an overweight position within our portfolios.

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