FRANKLIN TEMPLETON INVESTMENTS

Franklin Bissett Investment Management

As of October 31, 2018

Franklin Bissett Update on Dividend Income SMA/UMA Mandates

Good Relative Returns, Despite a Broad Equity Sell-Off

Amidst the recent broad sell-off in global equities, the Canadian equity market declined 6.3% in October 2018, its worst month since September 2011. Similarly, the S&P 500 declined 6.8% in U.S. dollars, also its worst month since September 2011. The bond market fared better as the general rise in interest rates took a pause in October. The Dividend Income strategy delivered favourable relative performance in this weak environment (declined only 3.6%).

While relative performance in its Canadian sleeve was meaningful, the U.S. performance was particularly noteworthy. Although the strategy's U.S. equities were not completely immune, the overall decline of the U.S. sleeve was a small fraction of the decline of the benchmark, representing exceptional relative performance. Long-standing exposure to more defensive sectors has been a headwind for relative performance of the portfolio through the course of this bull market (especially in the U.S.). Its Canadian holdings benefitted from a significant weight in Communication Services and Utilities, as well as its emphasis on Energy Infrastructure within the Energy sector and underweight in Materials and Industrials. In the U.S., outsized weightings in Consumer Staples, Health Care and Utilities provided some welcome stability and downside protection. As in the past, the U.S. continues to provide a natural complement to the Canadian component, rounding out some of the more concentrated sector exposures that are a structural feature of the Canadian equity market.

Although the portfolio has some meaningful positions in more cyclical businesses, our focus on valuation and a dividend emphasis also seemed to provide some insulation even within some of the weakest performing sectors. This was apparent in the U.S. Information Technology sector, where our holdings (Apple, Intel and Microsoft) outperformed their peers. And within the FAANG group, Apple was a clear standout in October despite weakness in the share price. Valuations have compressed meaningfully amongst this group, but with Amazon and Netflix down around 20% for the month, they are still trading with astronomical P/E multiples, leaving the potential for further downside if investors continue to lose confidence in growth projections.

A Time to be Discerning, Not Complacent

While the origin of this recent global risk-off environment may be debatable, we believe equity market excesses driven by investor exuberance regarding specific equities’ momentum and potential, rather than more deeply rooted fundamentals and valuation, is clearly evident. Furthermore, despite general optimism regarding the U.S. economy, economic storm clouds in some jurisdictions outside North America hold the potential to weigh on expectations for broader global economic growth. The United States-Mexico-Canada Agreement (USMCA) may bring increased clarity for Canada, but protectionism remains a critical global issue, especially between the U.S. and China. Also, the direction of interest rates carry enormous influence over the value of equities, and not withstanding the recent pause, interest rates have generally been on the rise this year.

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Leading into October, signs of investor optimism bordering on complacency, threatened to prove indicative of a late-cycle environment. Ultimately, equity market returns that are not rooted in the fundamental progress of the underlying business are generally not sustainable. And while impressive progress has been made by a number of constituents of the Canadian equity marketplace through the current market cycle, in several cases equity returns have gone beyond the progress of the underlying business. As was the case going into this most recent correction, we believe now is an important time to be increasingly discerning, not more complacent. With our long-term perspective and discerning approach, we remain ready to capitalize on equity market dislocations as they present themselves, and continue to build on our track record of superior absolute, relative and risk-adjusted returns.

Performance as of October 31, 2018 (%)

	1 month	1 year*	3 years*	5 years*	10 years*	Inception*[1]
Franklin Bissett Dividend Income SMA	-3.58	-0.82	7.23	5.25	8.87	7.65

*Annualized
[1]Inception Date: March 31, 1998.

IMPORTANT DISCLOSURES

The information presented is considered reliable at the present time; however, we do not represent that it is accurate or complete, or that it should be relied upon as such. Speculation or stated beliefs about future events, such as market or economic conditions, company or security performance, upcoming product offerings or other projections represent the beliefs of the speaker and do not necessarily represent the views of Franklin Templeton Investments. General business, market, economic and political conditions could cause actual results to differ materially. The information presented is not a recommendation or solicitation to buy or sell securities.

FOR ILLUSTRATIVE AND DISCUSSION PURPOSES ONLY. THE RETURNS SHOWN HEREIN ARE THOSE OF THE FRANKLIN BISSETT DIVIDEND INCOME SMA MODEL PORTFOLIO (the “MODEL PORTFOLIO”). From October 1, 2015 to present, the “pure” gross performance is based on a model account maintained by Franklin Bissett Separately Managed Accounts and assumes the following: (1) a portfolio size of $10 million; (2) the reinvestment of dividends and other earnings; (3) the effects of any corporate actions; (4) that the portfolio securities are valued daily using the most recent published end of day prices; and (5) no trading expenses. Prior to September 30, 2015 performance information presented herein are those of a model account maintained and reported by a third party dealer. The model account follows a similar investment strategy and utilizes the same research as the Franklin Bissett Dividend Income SMA model portfolio (the “Model Portfolio”). Accordingly, we do not represent that the model or dealer performance is accurate or complete, or that it should be relied upon as such. Actual client returns may differ for a variety of reasons including, but not limited to, differences in: portfolio size, percentages held in each security, the timing of purchases and sales, price per security, fees and expenses. These differences may result in returns that may vary from those presented. Performance is presented in Canadian dollars, assumes reinvestment of dividends and other earnings and is gross of fees. Taking into account fees would result in lower rates of return. Returns represent past performance. Past performance does not guarantee future results and may not be repeated.

Indexes are unmanaged, and one cannot invest directly in an index. They do not reflect any fees, expenses or sales charges.

Franklin Templeton Investments Canada is a business name used by Franklin Templeton Investments Corp.

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