Market Commentary
Second Quarter 2016

CI Investment Grade Bond Fund

Government bond yields globally continued to decline during the period. Sluggish economic growth momentum, modest inflationary pressures and expectations, low Government bond yields in other jurisdictions and a surprise vote in the U.K. to exit the European Union all combined to push 10-year yields in the U.S., Canada and Germany 25-30 basis points lower.

The Brexit vote in the U.K. on June 23, 2016 caused significant volatility in risk assets late in the period. However, spreads which had been reasonably stable after a strong "V"-shaped recovery in the first quarter rebounded sharply on bargain-hunting. The U.S. Investment Grade Corporate Credit Default Index (CDX) closed the period modestly tighter, while in Europe the equivalent index was seven basis points wider.

In short, the quarter was characterized by central bank caution about the path of economic growth, resulting in a further march lower in Government bond yields. Corporate credit, despite weak credit fundamentals and an uncertain earnings outlook, benefitted from buying by those investors seeking yield.

For the period, the fund underperformed its benchmark, the FTSE/TMX All Corporate Bond Index. The fund's duration (sensitivity to interest rates), on average during the period, was lower than that of the benchmark. Accordingly, the fund benefited less than the index from the decline in Government bond yields. Underperformance relative to the benchmark can also be attributed to the fund's exposure to European bank bonds. Following the U.K. Brexit referendum, European bank credit spreads widened. The index has virtually no exposure to European financial credits.

In our first quarter outlook, we expected Government bond yields to maintain a downward trajectory. Even after the continued rally in yields in the second quarter, we believe that Government bond yields have further downside potential. Weak economic growth and low inflation provide the key basis for this view. However, the importance of continued central bank balance sheet expansion (European Central Bank and Bank of Japan) which is causing interest rates to turn negative in these regions cannot be discounted as a force driving interest rates in North America lower. We project that 10-year Government bond yields in the U.S. and Canada will trade in a 1.20% - 1.70% and 0.80% - 1.30% range respectively. We would expect to add duration should rates back-up toward the higher end of these ranges.

Investment grade credit spreads have had a strong technical underpinning from significant foreign buying of North American credit. The hunger for yield is likely to continue to support this buying. However, this "relative yield"-based buying is widening the gap between credit fundamentals and

historic market valuations. In other words, investment-grade corporate credit spreads are looking overvalued. In our view, this is cause for concern as the underlying risk is increasing while the appropriate compensation is declining. It resembles, in some ways, the behavior exhibited by investors during the tech bubble era and the pre-great recession period in 2006. Accordingly, we are biased to increase the credit quality of our portfolio or reduce credit exposure outright on further tightening of credit spreads. CDX closed at 77 basis points at the end of the quarter. A narrowing of CDX to 65 basis points would prompt us to significantly reduce credit exposure.

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