Third Quarter Review and Outlook
Cumberland Income Fund
September 2016

Divergent Economies and Monetary Policies

The third quarter of 2016 gave us further indication of the diverging trends taking hold in the US and Canadian economies leading to a divergence in their respective monetary policy stance.

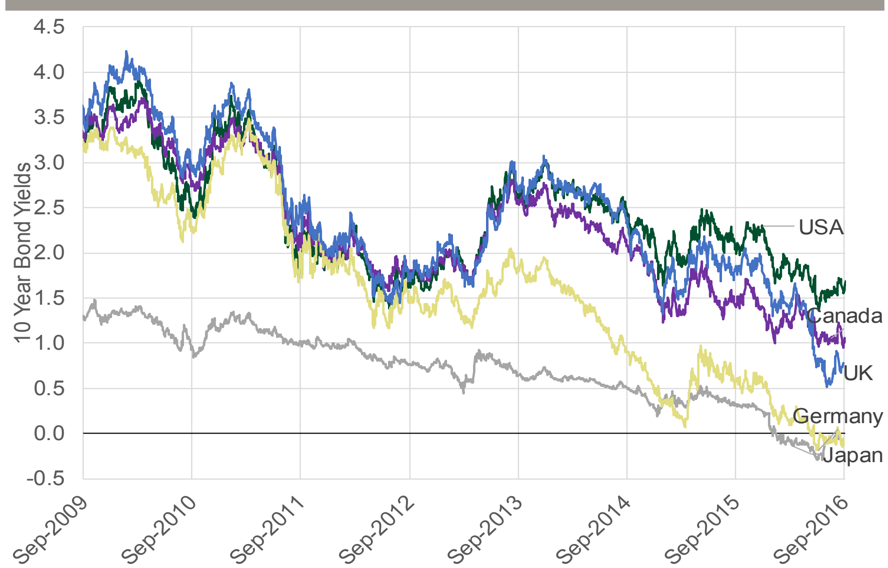
The US economy continued to grow, albeit at low-to-moderate growth, driven primarily by strong consumer spending. While business investments have been largely non-existent/detractor to growth for the past few quarters, we believe that a stabilization in commodity prices should see this trend reverse in the coming quarters. Various inflation measures still remain below the 2% target level while employment numbers have been strong bringing the US closer to full employment.

On the contrary, the Canadian economy is still undergoing a complex transition. The latest print of -1.6% GDP growth was impacted by the Alberta wildfires, without which the estimated GDP was approximately flat. Business investments have now been negative for six consecutive quarters, while exports are still undergoing a transition from energy to non-energy. Consumers have continued to hold up the GDP, but over-levered consumers and a recent softening of employment numbers in Canada are a cause for concern. Inflation has started to trend down as well with core inflation going below the 2% target.

Continued Structural Headwinds for Developed Economies

Developed economies continued to face structural headwinds of low growth and low inflation and there were no major changes to that outlook last quarter. G7 countries' year-over-year GDP growth rate of 1.25% as at Q2/16 remains very low while Europe and Japan continue to face disinflationary pressures, although signs of stabilization are emerging. Central banks, particularly in Europe and Japan, remained accommodative although in new ways (for example Japan's yield curve targeting) which continued to support lower yield environment across all developed markets. Post-Brexit, Bank of England cut its bank rate to 0.25% and announced quantitative easing with purchases of Sterling-denominated Government and corporate bonds. This was offset by an increased Federal Reserve rate hike probability and Japanese yield curve steepening efforts resulting in 10-year global yields trading in a tight range most of the quarter after giving back some of the Brexit-related lowering of the yield curve early in the quarter.

10 Year Government Bond Yields



Source: Bloomberg

Quarterly Update

As seen in the next chart, the US yield curve was higher by about 10-15 bps across the curve with the long end largely unchanged as the economy continued to show mixed economic data and Brexit concerns faded away – leading to further indication of a rate hike by the end of the year.

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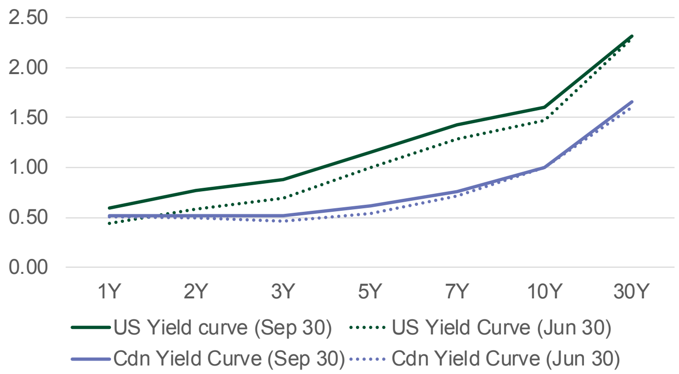
3 Month Yield Curve Change

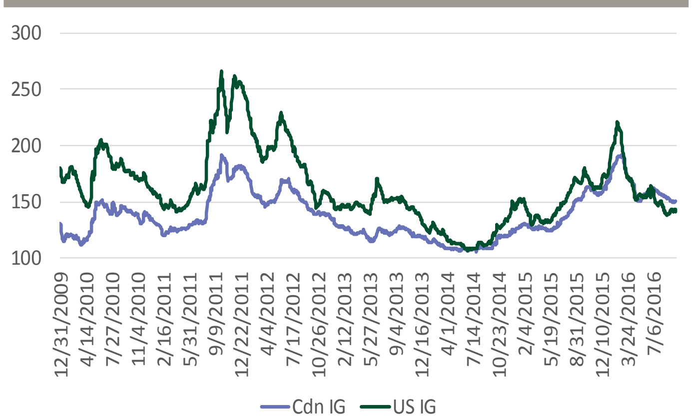


Source: Bloomberg

The Canadian yield curve was largely unchanged through the quarter reflecting the challenging economic data.

With regards to credit, demand remained extremely strong for investment grade corporate bonds as investors continue to reach for yield in this low interest rate environment. Demand for fixed income product remained strong as domestic fund flows continued to be directed into bond funds and balanced funds. In addition, international investors continued to purchase Canadian debt securities (including Federal, Provincial and Corporates). As such, Canadian investment grade credit spreads were tighter by approximately 19 basis points for the quarter, which is positive for corporate bond returns. US investment grade space also continued to tighten and was tighter by 11 basis points for Q3/2016.

Investment Grade Credit Spreads



Source: Bloomberg

For the quarter, the returns for various asset class indices were as follows:

Asset Class Returns as at September 30, 2016

Asset class	Q3 Return
Federal Bond Index	0.55%
Provincial Bond Index	1.53%
Corporate Bond Index	1.59%
S&P/TSX Preferred Index	4.66%
S&P/TSX High Dividend Equity Index	5.77%

Outlook and Positioning

We believe that the Fed is likely on a path of very gradual rise in interest rates as strong employment, balanced growth and inflation outlook is offset by a weak global economic backdrop and a strengthening USD.

On the contrary, we believe that Canadian growth and inflation outlook are tilted to the downside, which was also alluded to by the Bank of Canada. As such, we believe that the Bank of Canada is likely on hold until well into 2017.

Low sovereign bond yields along with the demographic trends in Canada are likely to keep fund flows strong into bonds and balanced funds, which will continue to be constructive for the fixed income markets – particularly corporate bonds. As such, we expect corporate spreads to continue to trend tighter (which is positive for spread returns). However, with more foreign investors buying Canadian debt instruments, there always remains a risk of a reversal of this flow which could create some volatility in spreads.

We remain overweight in corporate bonds and underweight in government bonds.

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Risks to Outlook

We continue to monitor the risks to our outlook. At present – the risks to higher than expected yields include higher than expected inflation trends, better than expected developed markets growth and a materials sustained rebound in oil prices. The focus is on the recent informal meeting (September 28), where OPEC came to an agreement to cut crude production to 32.5-33.0 million bpd; however, details need to be agreed upon at a formal meeting on November 30th. While the developments are supportive for crude oil prices, we believe that higher supply from non-OPEC countries would limit upside in prices. A stronger case for oil would likely take place if the production cut applies to countries beyond OPEC members. At present, we believe the current probability of these risks are medium.

Risks to lower yields include: a re-emergence of Eurozone growth concerns (Brexit impacts), growth concerns in US/China or a broader Canadian recession. We believe these risks are currently low-to-medium as well.

Some of the unknown tail-risks are a change in monetary policy mandates or the recent talks over "Quantitative Exhaustion". We believe these risks are currently very low and that central banks will continue to be accommodative but in different ways.

Gaurav Dhiman
Portfolio Manager, Fixed Income

Asset Allocation as at September 30, 2016

Asset Class	% of Portfolio
Cash and Cash Equivalents	2.8%
Government Bonds (incl. Floating Rate Notes)	18.6%
Corporate Bonds	53.7%
Preferred Shares	11.3%
Equities/Income Trusts	13.6%

Yield[1] Comparison as at September 30, 2016

FTSE TMX Canada Universe	1.71%
FTSE TMX Canada Government	1.46%
FTSE TMX Canada Corporate	2.36%
Cumberland Income Fund[2]	3.13%

1. Yield is the yield to maturity for bonds and current dividend yield for equities and preferred shares. Yield does not represent the total return of the Fund or the indices shown in the above table.
2. Gross of fees.

Cumberland Private Wealth Management Inc. is a leading independent investment firm that provides discretionary investment management and wealth management services for high net worth individuals, their families and foundations, with $1 million or more in investable assets. All of Cumberland's investment mandates are centered on building and preserving our clients' financial wealth. Founded in 1997, the firm is privately-owned by its employees and headquartered in Toronto, Canada.