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This is the Private Wealth Podcast with Manulife Private Wealth.

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PRESENTATION

Operator

Good afternoon, ladies and gentlemen. Welcome to the Manulife Private Wealth - A Focus on Diversification: Private Assets Conference Call.

I would now like to turn the meeting over to Glen Brown, VP and Managing Director of Manulife Private Wealth. Please go ahead, Mr. Brown.

Glen Brown, Vice President and Managing Director, Manulife Private Wealth

Thanks very much. Hello, everyone, and thank you for taking the time to join us today. As introduced, my name is Glen Brown, and I'm the Head of Manulife Private Wealth. On behalf of our team, welcome to the call.

It's been a dramatic few months on Wall Street, and while balancing risk and return in an uncertain world is difficult, Manulife Private Wealth's team remains focused on maintaining our approach to help clients protect and grow their wealth.

At Manulife Private Wealth, we have several interesting strategies aimed to help you navigate through these volatile times. Today's call will provide a deeper dive on one of these strategies, diversification.

Vineyards, farmland, commercial buildings; the wealthiest families have always owned private assets. In recent years, pensions and institutional investors, often called smart money, have followed their example by allocating to everything from timberlands to cranberries for diversification. In fact, Manulife has held private assets on its own balance sheet to add diversification, risk- adjusted returns, and downside protection from the stock market.

In this call, we explore the use of private assets, how they have a low correlation to public assets and can reduce volatility for investment portfolios. Joined by Frances Donald, Head of Macroeconomic Strategy, and Eric Menzer, Global Head of Pension & Fiduciary Solutions within the Asset Allocation Team at Manulife Asset Management, we welcome you to discover how Manulife Private Wealth can provide solid foundations during these volatile times.

We are recording this call, and a copy of the recording will be available to any participant upon request. If you have any questions or requests after the call, please contact one of our team at Manulife Private Wealth.

Our first speaker, Frances Donald, is a spectacular addition to the call, and is a pleasure to have her on again. She was nominated by Canada's business leaders as someone with one of the brightest minds in our industry, as listed by The Globe and Mail. She makes regular appearances on BNN and CBC, and is frequently quoted on the Wall Street Journal, Reuters, and Bloomberg. A valued member at Manulife, Frances is responsible for coordinating and generating global macroeconomic investment research and analyzing the potential opportunities and impacts on Manulife Asset Management's investments.

Today, Frances will share with us her insight on what the markets may look like in the next quarter. Frances, over to you.

Frances Donald, Head of Macroeconomic Strategy, Manulife Asset Management

Thanks, Glen. Thanks to everyone who dialled into this call. I'm sure, as Glen mentioned, we're all still reeling from the market that we've been witnessing over the last six months. I don't need to remind many people that we saw a, essentially, bear market occur in Q4 of 2018, but we have ripped right back.

Equity's up 22 percent; they hit their trough. This is certainly an environment marked by volatility. In fact, almost every presentation that I've been giving over the last couple of weeks has been 2019: A Year of Volatility.

While we probably won't see the magnitude of the sharp move that we witnessed in December and January occur again in 2019, that sort of pattern of sharp risk-off and sharp risk-on is one that we are expecting to persist this year and into 2020. That is a more difficult environment than we witnessed, pretty much over the past 10 years, and it's marked by a series of factors globally that I want to walk through today.

Thinking more short-term, however, over the next three to six months, and explaining a little bit about what has supported markets since January, I do believe that the V-shaped recovery that we've seen in risk has been supported by what I'll call three puts, or three supports.

The first one is a China put. It's some pretty significant stimulus that we've seen coming through from China. The second is what I'll call a Trump put, or a walking back of a lot of the trade tensions that we witnessed. The third is what I'll call the Powell put, or the move from major central banks, including the Federal Reserve, to step back on global tightening. These, combined, have essentially supported risk appetite and allowed for a pocket of risk-on and general complacency that we expect to persist for the next three to six months before things get dicey again.

In order for us to remain in this risk-on, sanguine, complacent environment, we do need three factors to stay as they have been over the last three months; we need three ingredients to remain risk-on. The first one is that we need government bond yields to stay calm and contained. We need central banks to continue to say, "We're probably done hiking."

The second thing we need is no new political or trade jolts, so no new headline news that the world is unravelling, or there is a massive trade war that we weren't anticipating.

The third is we need the global economy to stabilize. We need a lot of this fear of a global recession to dissipate. Now, we expect we will see these for the next several months; it's only really in the end of this year that we expect volatility to come back as these three ingredients dissipate.

What I wanted to do today is do a walk around the world, talk about how we're looking at the U.S., Europe, China, and then I'll finish with Canada. While we may not be, or one may not be directly invested in China or Europe, the reason I underscore these is because, in this environment, even a U.S.-only, long-only Portfolio Manager has to be aware that these global developments are having a significant impact on day-to-day risk that we witnessed in the Canadian and U.S. markets. Now more than ever, and particularly over the past 10 years, understanding the global economic picture is becoming crucial.

Let's start a little bit closer to home, south of the border in the United States. When it comes to volatility, one element is the story in the U.S. that we've been discussing heavily with our Portfolio Managers is the idea that 2019 in the United States, that it's likely going to progress in three stages. We're currently in the first stage, which we have named Data & Distortion. The reason I've done that is because the U.S. right now is very, very difficult to see a clear, underlying picture of momentum. What's really going on in the U.S. economy? We have almost no visibility.

This is because they've had significantly bad weather; they experienced a government shutdown in December and January; they have seen delayed tax receipts; we have witnessed heightened geopolitical tensions in December that really flowed through into the data. Most of the first quarter and the data that comes through, very difficult for us to get a read; that has created some choppiness in markets, and for us that's been an opportunity.

Now, as we come out of this environment, probably about a month from now, in April, we're likely going to see a kind of broad stabilization of what I call a Goldilocks environment, which is, the U.S. economic data is probably going to start looking much better, and it's going to be primarily driven by the U.S. consumer.

From our point of view, the U.S. consumer is not only the strongest spot in the U.S., it's probably the strongest spot globally: higher wages, big lumpy tax refunds, lower rates now on mortgages than they were dealing with a year ago. Those all support a strong U.S. consumer, and mean that's one of our favourite economic spots.

The U.S. is also benefiting from a significant amount of fiscal stimulus from tax cuts and deregulation. That's still in the pipeline for most of 2019, and we have seen corporate profits accelerating, which tends to be a great leading indicator for U.S. growth.

When we talk about volatility, where I become more concerned is, around September, around Labour Day. At this point, we do expect that addition recession fears will come back onto that docket. We began noticing the risk of a 2020 recession back in August of 2018.

Now, let me be clear: it is very, very difficult to forecast a recession this far out. In fact, I don't do it, I don't recommend doing it; we simply don't have the visibility. But we do know that 2020 is going to be a very hard year for growth, because we know that all the fiscal stimulus that we witnessed in 2018 and 2019 will run out very sharply, and we know the impact of higher interest rates in the United States are going to land, predominantly, about 18 months later, in the middle of 2020.

We also know that the impact of higher tariffs and trade wars probably land around that time as well. In the back half of 2019, we are expecting that recession fears come back onto the docket, and markets will likely see some movement around there.

Now initially, about a couple months ago, I did have some concerns that, as the U.S. economic data improves throughout the second and third quarter, that we might have to deal with the Federal Reserve to suddenly say they wanted to hike interest rates much more quickly. We're now pulling back from that view. In our view, the Federal Reserve is much less likely to raise interest rates now, again. They may actually be done for this cycle.

One of the reasons for this is the Federal Reserve has spoken a lot about average inflation targeting. Now, that might seem like a lot of technical comments, and we've had to read through a lot of papers from them, but essentially what the Federal Reserve is telling us is that they have missed their target of 2 percent inflation for so long, they're going to have to overshoot in order to average out 2 percent over an extended period of time.

This isn't the first time we've heard this from the Federal Reserve. They've talked about allowing greater than 2 percent inflation for some time, but we've never heard them talk about wanting to do it with such magnitude before. This is an important trend change from the Federal Reserve, that from our perspective, means they're much less likely to hike interest rates, even if the U.S. economic data does better.

That's one of the reasons why we like risk for the next several months, because we do believe that the economic data can accelerate, can do better, and the Federal Reserve is not likely to react to it. Of course, we are hearing from the Fed tomorrow, and we'll get some additional colour on that as well.

Let me move onto China, which I think has been an important global risk driver. We talk about China all the time in terms of its long run, decelerating growth and how this creates a headwind for global growth, and the risk associated with bad debt. But, let's speak a little bit more short-term.

Over the course of the second half of 2018, one of the big drivers of the selloff was it was the concern that China was decelerating much more sharply than it intended to. In the beginning of January, however, we saw sizable amounts of stimulus coming first from China, including, effectively, a rate cut. We now know that this amount of stimulus is likely to provide a stabilization in China's story, and that's relevant because it flows through to the entire world. It means that this headwind created by decelerating China speed (phon), and we can now actually see that provide a lift to Europe, for example, or to the U.S. as well.

However, one of my strongest concerns, and one that I think will essentially develop in the back half of this year, is that sentiment appears to be running ahead of demand from China. We were so excited to see stimulus; a lot of money flew into emerging markets. For example, a lot of money flew into Chinese A-shares, but it hasn't actually been justified by a stabilization of the economic data yet.

What we do need to see, in my view, is additional stimulus out of China in order to see China move from just a simple stabilization move into a V-shaped recovery or a U-shaped recovery. That might come in the form of these tax cuts in China; we are expecting VAT tax cuts and corporate tax cuts to come through, more local bond issuance. It may come from geopolitical tensions that look much more favourable.

It does seem like the market now is positioned for a trade deal and a more benign outcome, or at least the veneer of a deal, and that we can probably think that the worst of geopolitical tensions between the U.S. and China are behind us. But, we need to see a stabilization in the Chinese data, and probably some additional stimulus before I become very optimistic that this space can save us from a 2020 recession.

I also wanted to address the idea that, if U.S. and China reach a trade deal, that everything is good in the world. I am a believer that we should buy the rumour and sell the news on a trade deal in some sense. The reason for that is because the better the outcome of the U.S.-China trade deal, the less likely we'll see more stimulus out of China. This is a country that is not keen on reversing their deleveraging and de-risking efforts over the course of the last two years; I think while they're happy to make two steps forward, one step back, they are not keen on pushing two steps forward, three steps back. The better the trade deal, the less chance of stimulus out of China.

We also know that if the U.S. and China achieve a good trade deal, that's likely to strengthen the Chinese currency, which means that exports are not likely to do as well in that type of environment. I would also caution that, even if we see a U.S.-China trade deal, it's not likely that U.S.-China trade relations go back to how they were before this development. We're still expecting that Chinese businesses will face heightened uncertainties about future tariff and import restrictions, and that China will continue to see Capex declines.

Ultimately, China is really about a deleveraging effort as the government tries to rein in debt; that's the primary story there. While we might see another bump, three to six months of positive sentiment towards it, in the back half of this year as we head towards 2020, I do have concerns that markets will ultimately be disappointed.

Lastly, I wanted to touch on Europe, which is not an area that I have traditionally focused on but has become almost an obsession of mine. The Euro area has done very, very poorly over the course of 2018, and in many ways it's cheap—actually, Europe is always cheap, but it's cheaper than typical. It's actually, by a P/E ratio, about 10 years cheaper than it's ever been—or the cheapest it's been in 10 years, excuse me.

The Euro area has done very poorly in 2018 because it is an economy that has been dependent on external demand. As the rest of the world has slowed, as China slowed over the course of 2018, it suffered. Its Capex cycle turned downwards, corporate profits deteriorated, tighter financial conditions have been very difficult, and it's also been an area that has disproportionately suffered from trade war uncertainty, which has undermined the demand for capital goods.

Now, in Europe, Europe is actually undergoing a manufacturing recession at this point, with Germany floating close to an actual recession. We have concerns that some areas of Europe would slip into recession. In 2018, they appeared to have narrowly avoided that.

There are now some reasons, however, to be more enthusiastic about Europe, and while I have concerns margins have gotten ahead of themselves on pricing in a positive China story, I think that there's more good news to come out of Europe than bad. We know that the central banks have extended forward guidance, they are now likely to be on hold at least through the end of 2019. I don't think this is a central bank that is going to be hiking rates at all.

We know that there is some fiscal stimulus that could come through the pipeline in Europe, particularly in Germany, and we know that that China stabilization, which should occur in about the next three to six months, will filter through to Europe by the end of the year.

The only reason I'm holding back my enthusiasm in Europe just a little bit is because there are some tail risks, and if they do occur, they could be quite damaging—one of which is the possibility that the U.S. levies auto tariffs on Europe in particular, that's also damaging for Japan. If they do that, depending on how they construct it, it could shave as much as 0.6 percentage points off of German GDP, or 0.3 percentage points off of Eurozone GDP in total. That's sizable.

Then of course, we have to deal with Brexit issues. Brexit now looks as though it will be postponed. We don't know how long; estimates range from two months to two years, but this is an issue that is going to remain front and center.

The possibility of auto tariffs, of Brexit issues, of trying to get to a resolve on the U.S.-China trade relationship, which doesn't appear that we'll see anything concrete until May or June, this means that we continue to be in an environment with heightened headline risk: one difficult news bulletin away from seeing a sharp market selloff on any given day. That's a very difficult environment and it's one that we have to manage around.

On Canada, a couple quick notes. As you know, today is the Canadian Federal Budget, and when I finish this call I'll be hopping over to BNN to give a live reaction for two hours; you can tune in and hear what I have to say about that. I don't have a poker face, so if I'm unimpressed, you will see it.

Canada right now; up until about a month ago, our impression was the Bank of Canada would still be hiking interest rates. This is, in my view, the most hawkish central bank around. This is a central bank that is very keen to normalize interest rates as soon as possible and slowly deflate the debt bubble that has arrived in Canada. But they too have capitulated in their most recent policy status, and as of about two weeks ago when we changed our view that the Federal Reserve would no longer hike interest rates, I no longer believe Canada will be able to do that either.

One of the problems for Canada, and particularly for the Bank of Canada, is that this is a central bank that have acknowledged exports were weak but business investment would reaccelerate, and consumer spending would hold strong.

Unfortunately, that doesn't appear to be what's happening. Canada, after the U.S. had extremely strong two years, exports have been lacklustre out of Canada. This shouldn't happen. If exports in Canada can't reaccelerate when the U.S. is on fire, then they're not going to accelerate when the U.S. falls into an almost-recession or a full recession in 2020.

One of the more disappointing elements of the Canadian story is that business investments, even after we got at least a pseudo-resolution on NAFTA or USMCA, it's still falling. What's on in this environment is that survey data continues to tell us that companies want to invest; companies tell the surveys, we're interested, we want to move forward. But, the actual hard data is telling a very different story.

Then I think what was most disappointing to the Bank of Canada is that consumer spending is faltering very, very quickly. I remember last time I had this call with this team, we talked about what would happen as interest rates rise in Canada, and I talked about something called the debt service ratio, which is essentially the share of income that everyone brings home that they put towards the interest and principal on all of their debt. For the last 10 years, it's been hovering around $14, which means that if you bring home a hundred dollars, $14 of your $100 goes towards paying the interest and principal on your debt. For 10 years, it's been about stable, in large part because, as our principal portion has risen, the interest component has fallen.

But now, it has risen sharply, to $15, which may not seem like a big deal, but it really is. It means that, about—out of $100 that every Canadian brings home, they now have to allocate one more dollar towards their interest and principal on their debt, which means that $1 is coming out from some other area in the economy. Now, at first it was savings rates, but the savings rates are pretty depleted. Now we're seeing retail sale spending fall; that I expect to see continue.

Next up would be auto sales, which have been very weak, and my best leading indicator for what happens to housing. This is the biggest problem for the Bank of Canada, that as those costs of interest rise for Canadians, they cannot spend in other areas of the economy, and this slows the economy more sharply, I think, than they have been understanding.

Big picture, I do want to reiterate that, for the next three to six months, we do have some support from China stimulus coming through, better geopolitical headlines for a brief period of time, and central banks that appear to be on the sidelines. But, if we continue through this kind of nice patch for three to six months, in the back half of the year we are facing a return to geopolitical risks that will be heightened, concerns about 2020 recession, and likely consumer spending that continues to feel the drag from higher interest rates.

I'll remind you, in order to remain in a risk-on environment, we need three ingredients. This is my recipe for risk-on: government bond yields that stay calm and contained, no new political trade jolts, and a global economy that needs to stabilize or reaccelerate.

I'm going to leave that here. Thanks for having me on the call, I appreciate it, and I hope you all enjoy the Federal Budget today, think it’s exciting for economists.

Glen, I'll pass it back to you.

Glen Brown, Managing Director, Head of Manulife Private Wealth

Thanks very much, Frances.

Our next speaker is the Global Head of Pension & Fiduciary Solutions within the Asset Allocation Team at Manulife Asset Management. The Asset Allocation Team is responsible for the development and growth of Manulife's Asset Allocation solutions for both individual and institutional investors in the United States, Canada, and Asia.

Eric Menzer leads a team responsible for the portfolio management of Manulife's U.S. and Canadian employee pension plans, U.S. health and welfare plans, and third-party DB, advisory and fiduciary-managed solutions.

Thank you for joining us today, Eric, and over to you.

Eric Menzer, Global Head, Pension & Fiduciary Solutions, Manulife Asset Management

Thank you very much, Glen, for that introduction. I very much appreciate it. As Glen noted, I'm part of our multi-asset Solutions Team, and I am here today to talk to you folks about private assets.

Now, we are very much consumers of private assets within our multi-asset portfolios, particularly our institutional mandates, as well as our internal pension plans which we run here, and various outsourced CIO mandates as well. As an organization, we have been running private assets for quite some time, going all the way back to the 1930s.

I want to spend the next 15 or 20 minutes just kind of touching on who the key users of private assets are, talk a little bit about some trends in the marketplace that we're seeing, as well as the different types of private assets that we might consider, and ultimately, the benefits and uses of those private assets within your portfolio.

It's no surprise that I'm here today having this conversation, as we have quite a bit of conversations with our clients on a regular basis with regards to private assets. We see the demand for private assets picking up; it continues to gain in popularity. As you know, the amount of products that are out there on the marketplace is increasing as well. There continues to be more and more ways for investors to gain access to these investments, which by and large, historically, were reserved primarily for the large institutional investors.

If we go back, we see endowments and foundation using private assets for quite some time; the allocations to private assets and real assets within those plans are typically very, very high. We see them as high as 40 percent to 50 percent. They're there to meet various needs, particularly spending rate needs, and income needs that those organizations have.

In defined benefit pension plans, we've seen, obviously, quite a bit of use of private assets there too, both in Canada and the U.S. and globally, particularly as the liability-driven investment type of strategies have gained in popularity as pension plan's funding status positions have improved. Lots of pension plans are looking for ways to not only lock in those funding rates but provide themselves with lower volatility and stability of income within their pension plans. That's the primary reason of what we use them for within our own pension plans.

We've seen family offices pool assets together to gain access to private assets for higher returns. Now, as more products become available, we're seeing high net worth individuals and the mass affluent market really looking to gain broader diversification, given the environment that we're in, and as the products are available to hit that.

I want to read an excerpt from Chief Investment Officer Magazine that I came across recently when I was tasked with speaking with you folks today. There is a piece, on January 31, that read "Alternative investments made up the biggest part of the typical family office portfolio in 2018." This was a study, a research performed by Peltz International.

They surveyed 21 family offices and they found that alternative investments made up more than 52 percent of family office portfolios, compared to 22 percent for equities and 15 percent for fixed. This was up from the firm's last survey in 2016, where alternatives made up 41 percent of a family office portfolio. We see the increase, obviously, in alternative investments within the high net worth, ultra high net worth family office space.

We've seen this trend play out in the institutional defined benefit and DC assets as well. For those of you that are familiar with Greenwich Associates, Greenwich Associates puts out their annual survey, and this past year, roughly 25 percent of Canadian institutional assets were in some form of private asset, via infrastructure, real estate, or private equity. That's up from 11 percent in 2006; over the last 12 years, we've seen a greater than doubling of plans moving assets into private assets.

To further that research, as they surveyed their plan participants and institutional investors, in terms of what the expectations are in the asset shares over the next three years, we have a staggering amount of respondents putting out there that, in the 20 percent to 30 percent of respondents looking to increase allocations to infrastructure, real estate, private equity, as well as real estate fund-to-funds, and consequently are looking to significantly decrease their exposures to Canadian equities.

Now, where's the money going? What are they looking to put those monies into? Well, what are the different types of private assets that you may consider for yourselves? Historically, we've seen a lot of conversations around direct real estate. Now, direct real estate, in terms of the private assets, has been around for quite a bit. It's had popularity and it's had the applicability and vehicles available for investors to gain access to, and it's an easy conversation to have with clients. There's a level of familiarity that exists there, with real estate, given that obviously we all—most of us own our own homes and can certainly understand return drivers that drive real estate returns, particularly with income by rents or capital appreciation and improvements.

Where it gets more difficult and it gets harder to have the conversation or extend the conversation, it gets into some additional types of private assets that gained quite a popularity here within the last decade, and that's within farmland, as well as timberland investing, infrastructure investing. Things like transportation, and obviously private equity, becomes a little bit harder, or not as familiar for folks to understand, but there's significant value that can be driven here from these particular assets in terms of an addition into a multi-asset, multi-manager type portfolio.

When we talk about farmland, we're talking about crops; we're talking about permanent and row crops, things like almonds and pistachios and walnuts. We're talking about corn and soybeans, things that are driven by, obviously, appreciation of land values but also sensitivity and drivers of commodity pricing.

With timber asset investing, timber asset investing is driven very much by pricing and lumber pricing. This is owning various species of trees throughout the geographies that are used, and really driven by the homebuilder market, can add a significant value and diversification benefit into the portfolio.

When we talk infrastructure, things to look out in infrastructure, various types of strategies that are out there are gaining exposures and assets to utilities, contracted utilities and pipelines, power and wind farms. Within infrastructure, a sub-infrastructure asset class of transportation includes things like air, rail, and Maritime investing.

We've seen a whole host of strategies become available in the marketplace over the years that have extended beyond the traditional public equity and public fixed income, and extended beyond what folks are familiar with, with traditional direct real estate, into some of these other areas that have proven to provide some significant diversification benefits into the portfolio.

Some of the key drivers that are driving folks into these assets, traditionally, is income. As we look at the yields within government bonds and within corporate bonds, as investors look to maximize return, they're shifting out of what we see as traditional fixed income, in some cases, into alternatives because of the yield pickup that they can get in there. If we look today at the Canada 10 Year yield, we're looking at roughly 1.9 percent, and we're looking at Canadian corporate bonds yielding roughly 2.6 percent.

If you shift over into Canadian real estate and infrastructure, you're looking at yields up in the 5 percent and 6 percent range, in some cases. There's a significant yield pickup, to move out of your traditional fixed income into some of these alternative investments, and to do so with very similar volatility.

These assets are typically perceived as high quality in a lot of cases, particularly with farmland and real estate where there's predictable cash flows. Similar to fixed income, we're looking at long-term leases that are contracted, and there's less variability in those cash flows for investors to look at.

What we have seen as a result of the flows and the demand moving into alternative investments that have—valuations have compressed. It is becoming harder and harder to find value within these assets, but the value is still there, relatively speaking, compared to equities and fixed income, and has proven to add on a risk-adjusted basis.

I did send out a few slides; I'm not sure if most of the folks have gotten those slides on the call. If you don't, that's fine, but if you do, there's a couple things I've put in there just to highlight—I think it's important, the various requirements and considerations as to why clients might consider private assets within their portfolio. We like to break that out, really, into two categories, and that's diversification seekers and income seekers.

When we're thinking about that, we're thinking about lower volatility, we're thinking about lower correlations, and we're thinking about higher levels of income. That of course doesn't come without its sets of challenges. For those of you that have spent some time in this space, you're more than aware that gaining access to these types of investments can be very challenging. There are very much, supply constraints and a huge amount of demand that is piling up, and queues that are building up while trying to get money put to work in these asset classes.

Frankly, there's obviously the liquidity aspect of the equation to consider. As we go into these assets, a lot of these assets typically have long-term lock-up periods that can extend out as long as 10 years or more. It's very critical to pay very close attention to the types of strategies that you're looking at in terms of how that meets or stacks up against your liquidity requirements that you have in your portfolio.

There are the introduction and accessibility now of more and more, of open-end type fund structures out there in the marketplace. It's becoming more of an ease of gaining access from a liquidity standpoint, where the pension plans and endowments typically have been in a position to be able to have their money locked up for very, very long periods of time. That might not be the case as we start to move down market into the high net worth, ultra high net worth individual investor category that may not need immediate liquidity but may want to have slightly more liquidity considerations there than to have a 10+ year lock-up in their portfolio.

There is a slide I sent out that is titled Diversification Seekers, and we use timberland as an example here. It's a pretty common chart; it's not something that's new here, but it very much drives home the point of the risk and return, the risk-adjusted return comparability to public fixed income and public equities.

It's no surprise here as you see the various drivers of return. Putting timberland up here on the top left-hand corner of the page, which basically puts it in a low 6 percent, 7 percent volatility with an 8 percent to 10 percent return type range. That can be very, very attractive over time. Granted, this particular chart is a historical chart. When we think about how these assets are expected to perform in the future, we certainly are expecting lower returns in the future. Our analysts are forecasting lower returns going forward within alternatives, but also within public equities and public fixed income—so there's very low return hurdle on Canadian large caps at 7.5 percent, and on international equities it's 7 percent. If you compare this to investment-grade corporate bonds at 2.5 percent, we have investments here that can return upwards in the 7 percent to 12 percent range with much lower volatility. Even though it's lower than historical standards, it still proves itself to be a very attractive investment to add into the portfolio.

In addition to the risk-adjusted returns and the benefits that private assets add to the portfolio, there's the idea of correlations. For those that have looked at a correlations table or looked at various correlations tables out there, there's quite a bit out there. But the important thing to look at is not just the correlations of private assets individually, to equities and fixed income in a balanced portfolio, but also looking at the different types of private assets and how they compare to each other—which has been proved to provide even further diversification benefits beyond a single strategy like adding real estate into your portfolio.

As folks take the step beyond traditional direct real estate in their portfolio and start to look at additional assets like infrastructure, timber and farmland, you'll see the correlations come down quite a bit. For example, when we look at timberland and farmland relative to global bonds, we're seeing negative correlations. Relative to equities, we see only slight or low positive correlations. Then when we look at individual private assets to each other, for example, infrastructure versus farmland, there's a negative correlation.

There's quite a bit of additional benefits that can be had by adding additional private assets into the portfolio, beyond traditional direct real estate that a lot of folks typically already have in their portfolios.

Now, there's another slide that I sent out that has to do with the income. It's titled Income Seekers. For those of you that don't have it in front of them, it's basically a chart that goes back to 2006 up until 2018 and highlights the farmland returns in the U.S. over time and breaks out how much of that return has come from income and how much of that return has come from appreciation.

The attractiveness of farmland and other private assets has to do with that, and in a lot of cases you'll see that more than half of the return is coming from income. In this particular chart, you'll see upwards of 50 percent to 60 percent of the return being driven by income. When you look at real estate, you can get as high as 80 percent coming from income.

The income component of private assets becomes very, very compelling as an alternative to fixed income. It certainly helps individuals and income requirements, but also institutional investors meeting their spending needs, and particularly when we look at defined benefit plans, making benefit payments and including these assets into longer-term liability-driven investing strategies that can help get these liabilities or pay liabilities. It very much helps smooth out the rise in the returns and provides a very attractive investment set.

In summary, we've talked about risk-adjusted returns, we've talked about the income and obviously the correlations, but some things to consider when you're looking at private assets. These assets, as we stated, are long-term investments, so it's important to target strategies that you really have a high conviction on. It's important to find the right partner to gain access to scale. Not all of these strategies are created equal, in terms of the terms of these particular deals, in terms of the fee structures that are associated with these deals. It's very, very important to pick the right one, because even if it's an open-ended strategy, you're going to be committed to these assets for quite some time. The encouragement is to do the work upfront and make sure that you get it right from right out of the gate.

The other thing is focusing on income strategies, even in economic slowdowns, and high-quality assets, can look at assets that have contracted cash flows that should pay out over time will help to provide some stability, even in different economic environments.

That concludes my formal comments. From there, Glen, I want to thank everyone for having me on this afternoon. I'll now turn it back over to you, Glen.

Glen Brown, Managing Director, Head of Manulife Private Wealth

Thanks very much, Eric, really good insight.

The team here at Manulife Private Wealth remains focused on helping our clients protect and grow their wealth, and through this call, we hope you are able to better understand some of the use of private assets and where to position them within portfolios.

At Manulife Private Wealth, the client's access at a lower entry-level, a suite of exclusive, real asset classes which strive to deliver diversification and growth benefits to complement their overall investment portfolio. If this is of interest to you and you want further information, I would welcome you to reach out to any of the members of the Private Wealth Team.

Thanks once again for taking the time and we hope to see you again next quarter. Thanks very much.

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