Tuesday, June 23, 2020

This is the Private Wealth Podcast with Manulife Private Wealth.

Speaker Participants

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Presentation

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

Hello everyone, thank you for taking the time to join Manulife Private Wealth's virtual call: The road ahead, focusing on your investment goals amidst uncertainty. I'm pleased to welcome our speakers to the upcoming segment: Francis Donald, Chief Economist, who will provide a market update and insight on navigating the next chapter of COVID-19, and Jamie Robertson, Senior Portfolio Manager, Head of Asset Allocation, who will put into context the short-term volatility we are currently experiencing and the impact it has on investors' long-term saving goals. To those interested in a replay or sharing contents of this call with others, we are recording this segment and a copy of the recording will be available to participants on our new site, manulifeprivatewealth.com. If you have any questions or requests after this call, please feel free to contact a member of the Manulife Private Wealth team and we're pleased to help you. Many countries around the world, including Canada, are gradually reopening their economies as COVID 19 infection rates slow. While this progress towards normalcy inspires a sense of cautious optimism, overall uncertainty remains high, and investors find themselves sitting on the sidelines, holding cash generating little or no income. As long-term investors, it's important to look beyond the current uncertainty and think about the next two to five years. Our first speaker, Francis Donald, is the Chief Economist and Head of Macroeconomic Strategy at Manulife Investment Management. Leading the macro research team, Francis is part of Manulife's Global Asset Allocation team's development of asset class forecasts. She's responsible for coordinating and generating global macroeconomic investment research and analyzing the potential opportunities and impacts on Manulife's Investment Management's investments. Today, Francis is going to share with us her insight on key macroeconomic themes and market outlook for the next quarter. Francis, over to you.

Frances Donald, Chief Economist and Head of Macroeconomic Strategy, Manulife Investment Management

Thank you so much, Glen, and I wanted to apologize. I'm not on video today and the reason is well I told everybody it's because my power is supposed to be shut off this afternoon but really, it's because I'd like to do this in my pyjamas just like every other call. No, I'm kidding, apologies for that. Of course, work from home always creating challenges. The biggest challenge that I see on the day-to-day is that I continue to hear so many stories about what the post-COVID world will look like. Everybody talking about work from home, or whether we're going to see the economy reopen, or do we see credit defaults rise. And one element of the story that I find has been particularly complicated for just about everybody, including myself, has been getting the timelines right. When will everything happen and in what order? So what I wanted to do today is not so much be a crystal ball that tells you exactly what will happen and what market will move on any individual day, but try to provide for you a framework for how to think about what's going to occur in the next three months, one year, five years from now. I will tell you this is actually a lot of good that is happening in this economy, and of course the market is reflecting a lot of that. There is also no shortage of bad. What's very interesting about the current environment is we believe the bulk of the good will actually occur first, whereas the bulk of bad will be backloaded. So the way I want everybody to think about the recovery is not in the standard, "What letter it will be?" I'm sure we all hear this every day, will we have a V-shaped recovery where we see a rapid reacceleration? Will we have a U-shaped recovery where there is a slow rebound and then we get back to normal.? Will it be an L-shaped recovery in which we just sort of stagnate at very low levels, and then you have people getting fancy and coming up with Js and Ps and all sorts of other stuff. My recommendation is to throw those letters out. They are too simplistic and they result in people making mistakes, not just with markets, but the way we think about the macroeconomy. Instead, I want to introduce to you a different way of thinking about what's going to occur in the post-COVID world and the way I'm going to suggest we think about this is in three phases. The three phases are, number 1, a rapid rebound. This is the phase we are in now, it will last from now until August-September. Phase 2 is what we're calling the stall-out. The stall-out goes from about September and may last up until a year, maybe even 18 months. And Phase 3 is what we're going to call the new normal, it starts in about three years, and then is that world on an ongoing basis? So let's talk about each one of these phases and what we can expect in each one, and my hope is that when we finish talking in these 10-15 minutes or so, as you read articles, whether they're in the Globe & Mail or you see an interview on BNN or CNBC, you'll be able to categorize the content being discussed into its appropriate phase. And if we can start by getting the timelines right, then we'll be better investors as a whole. So let's start at the beginning, Phase 1, what we're calling a rapid rebound. A lot of people saying this is a V-shaped recovery and certainly for now it is. Now we and my team and of course much of the financial profession is no longer using data points that in the past we would have seen as a leading economic indicator. Monthly data like retail sales is now too slow. It doesn't incorporate the speed at which COVID-19 has absolutely decimated our economy and it isn't fast enough to tell us when we're coming back online. So instead what do we do, we use new data we've never used before. Google mobility data, how many people are going through the PSA passenger lineup? How many people made reservations on the open table website? We look at this every single day, and all of that data told us that the worst of the drawdown in economic growth actually occurred by mid-April, and we have been rebounding in the economy since mid-April. That's about two months ago that we probably saw the bottom in that second derivative. What's hard, however, is that a lot of our monthly data is only telling us what happened in April or May. It is lagging. Now from this rebound that we've seen in general activity, how people are moving around, we know that this economy is actually coming back online really quickly. Now when I say it's coming back online, I don't mean we're going back to pre-COVID-19 world, I mean that we're about to recoup, in our estimate, 60 to 70% of what was lost in March and April will come back online by the end of the summer. And just as March and April produced the worst economic data points that we have ever seen in our lifetime, the coming months are going to produce the best economic data points that we have seen in our lifetime. That's things like the U.S. jobs report, the Canadian jobs report, this morning's U.S. retail sales numbers. Just about every monthly or weekly data point we're going to get is going to be the best ever. Of course, this is a compressed recession, it happens faster than any recession we will recover mostly as fast as we ever have. Now in this period when we see this rapid rebound, one of the reasons why it's been so aggressive a rebound is that we see record levels of fiscal policy and particularly transfers direct to households. So there is a large segment of Americans who did not lose their jobs or separate income declines. They also received income support and those who did lose their job, we estimate that somewhere between 30 to 50% of their lost income has been immediately supplemented by government transfer. So that implies that even though we have the record high levels of unemployment, the hit to the economy is perhaps not as initially difficult for the economy as well, and at the same time, of course, we have extraordinary levels of monetary policy support that is helping things like rate-sensitive sectors like U.S. housing and flooding the system with liquidity. Of course, liquidity of cash on the sidelines, it has to go somewhere heading straight into stock. So we have this estimate that in the next few months the market will be enraptured by this better economic data, and in my view, most economists, the kind of old-school economists we might think of, are probably behind on estimating just how ferocious this initial rebound will be. Now of course my initial rebound thesis from now until August-September is not without weak points, and there are things that could absolutely trump that and they include we're beginning to see some elements of this if COVID-19 comes back earlier than expected. Market grappling what that means right now in a couple of U.S. [INAUDIBLE – 00:13:25] and if we were to see a policy mistake and by that I mean if the U.S. government does not extend unemployment insurance that runs out in July. We're already seeing in Canada that the Prime Minister is extending the Canadian Emergency Response Benefit, recognizing that they need to continue that stimulus. So that might sound very bullish, and in some ways I think I am and the market has already started to reflect some of this, but here's the challenge: We then enter a period that will be much more difficult ,and this I think starts probably around August or September. We call this the stall-out phase, Phase 2. Now this is a phase where I actually go from being someone very bullish on the economy to much more of a bear. Now I think I've been very vocal, and anyone who will pick me I will tell you that I have some concerns about what happens next. Remember, the first phase of this rebound is about 60 to 70%. We still have another 30 to 40% of growth that we have to recoup and this is going to be more challenging, and it's challenging for a couple of reasons. Number 1 is governments have been clear, particularly in the United States, that even if we were to see an extension of some of our policies like transfer checks or stimulus checks, it is still possible that we see a lot of the fiscal stimulus expire. If unemployment insurance is topped up, it's likely to be topped up by less on an ongoing basis, so really that fuel that contributed to the rebound in phase 1 is now starting to dissipate. Number 2 is that we know a lot of companies are coming back online, they are technically open for business, but they are operating at reduced capacity. So think about a restaurant that now has to separate its people, they cannot take in as many people, and as a result, it gets less revenue. My hairdresser, nothing is more important to me than the world than not discovering that I'm actually a brunette and not a blonde. I think time is running out for me on me on this one. I called my hairdresser and he said, "Listen, even when we reopen again, we'll have to take a reduced amount of people. We can't offer blow drying services," which is very problematic for me, of course, "and so we actually can't charge you for a blow dry and we're going to have few people coming in." Well this is just one example of companies that are actually going to be reopening, bringing people back into work but taking in less revenue. Now one of two things is going to happen here or both. Either they will have to raise prices so my hairdresser will say well we won't give you a blow dry and we're going to charge you double for that haircut or they suffer less revenue activity both of which are painful for the economy and my sense says when we look at the data, there will not be a large enough price increase to offset the decline in revenue. So you might have heard me talking on various channels about an economic second wave of insolvencies in Canada and the United States, and this is my concern, that we are operating at reduced capacity, revenues decline, and prices are not growing enough to offset that. Now I also worry about unemployment. We do know that there is a whole wash of companies that did go bankrupt over this period. Every day I open up the news I see new ones whether it's Hertz or J. Crew or Gold's Gym, a variety of Canadian retailers have already gone under. Now those people who lost their job are not getting them back. One of the challenges we see is the longer people have been unemployed, the more painful it is for the economy. A, their personal finances start to decline, but B, the duration of unemployment actually is a pretty good indicator of how long someone will get back in, or whether someone will get back in. If you've been out of the labour force longer, you're less likely to have relationships, so your skills might not be up to date. It's harder to get rehired right away. So in this second phase of fallout, I'm worried that we have sticky high unemployment and we struggle to get that down. Now I am talking about the second half of the year, and there's a couple things that might happen in the second half of the year, one is the U.S. election and that will carry additional risks, things that we need to watch particularly on a sector-by-sector basis, and we are likely to see more between U.S.-China trade tensions either before the election or right after it depending on the election outcome. I am concerned about a COVID-19 second wave that comes through in the fall, and to be clear, what we're witnessing right now in the United States is not a second wave, it is a continuation of the first wave. So if we actually eradicate COVID-19 pretty aggressively and then it comes back to life in the later part of the year, that's problematic as well. So I am concerned about the second period, the stall-out, and I do notice that there is a struggle among a lot of commentators to differentiate between how good things will look in the near term and how challenging things might be a little bit farther out. And then of course we get to Phase 3, which is what we're calling the new normal. Now the new normal to me are all the interesting developments that COVID-19 has amplified or accelerated that are likely to change the way we think out five years or longer. Now I sit with the asset allocation teams, I work very closely with Jamie Robertson which is a pleasure I have to tell you, and one of the things that we think about is what does the five-year outlook look like if we think about our longer-term investment strategy. And here, COVID-19 has probably acted as an accelerant on a lot of the trends that we knew were already in the works, not an event or a shock that radically transformed our view. It just brought forward several important trends closer to us now. Maybe moving things that we thought would take 10 to 15 years into the 3- to 5-year horizon. Some of these include, most importantly in my view, deglobalization. So deglobalization was a trend that was already occurring as we saw a lot of countries, not just the United States but the U.K., several European countries, even many Asian economies, saying this conflict of free trade maybe isn't good as we learned about in all of our textbooks, maybe we should apply tariffs and tariffs will actually generate different economic outcomes. But tariffs were the first deglobalization shock. We're now experiencing a second deglobalization shock and that is your supply chain coming out from Asia, maybe you're sourcing notebooks or labour or some intermediary parts. That's not the first time it's been disrupted. Now it's the second time for an entirely different reason, and that's a health crisis, a pandemic. So what we expect is that many companies, whether they're new or old, are going to be questioning, should we really have these supply chains that extend outside our nation's border? Maybe it's worth it to pay more for local goods and services, and while that might sting in the short time, it's almost like an insurance policy against the risk that, you know, there's a third type of globalization shocker or another pandemic or a new government that feels equally strongly that we should be applying tariffs. Now if we do see deglobalization in companies make these choices, a couple things are going to happen. No. 1 is that supply chains will shift and that will have sector implications. No. 2 is that we may see regionalization through the form of trading blocks. I think in this particular case, Canada is likely to do more business with the U.S. and less with Asia even though they talk a lot about diversifying. And 3, we probably will see some forms of inflation in certain goods as we raise prices to have more locally sourced goods and services and labour. No. 2, which I think is critical here, is that we are seeing excessive, I shouldn't say excessive, extraordinary levels of government debt. The U.S. is facing its highest debt-to-GDP ratio ever, mind you this goes back to 1800, it has never seen this high level of debt. There's two ways to get out of really high debt-to-GDP levels. One is to just grow your economy more. If you can get better growth, then you're actually fixing the denominator on a debt-to-GDP, raise the GDP and all of a sudden, your ratio looks better. That's challenging now, particularly in a world where we've had slower growth over time and deglobalization is likely to take hold, so instead what we might be facing is well, a lot of people who are calling for fiscal restraints, you may absolutely see calls to government to everything from, you know, raise revenue, i.e. taxes, or cut spending. Now we're a ways out from that, but it is something that we need to think about now. Now one thing that's particularly important when we have these huge amounts of government needs and spending is that these governments have to issue debt, they have been doing so and in doing so, they have pushed out a lot of supply into the long end of the treasury curve in the United States and Canada, and that is creating the steepening of the curve that we expect to continue on a several-year basis. And yet, I can spend this time talking to you about work from home and corporate real estate, all of which as an aside I think are overdone themes. BMO's important theme coming out of this story is that interest rates have been pushed to zero and they are likely to stay near zero for another five years or longer. We do not expect any major central banks, in Canada, the federal reserve, the ECB, to be raising rates over the next five years. Now unfortunately what this does is that it means that we have an even larger share of global government bonds that are either negative yielding or yielding very, very low. If you're thinking out over a five-year horizon as an investor and you're looking at global bonds based on our estimate over the next five years in Canadian dollars, you're only getting 1.4%. That's quite low, it's very difficult for you to generate returns that you need to just by being in something like a global government bond. So what are we witnessing? We're witnessing a lot of money that needs to go somewhere to get some sort of yield or return. As a result, it's flooding out the risk curve into things like equities. Now on our team, in the Canadian Asset Allocation team, for us that means thinking outside the box, sometimes it means alternative investments like infrastructure are weak. It means thinking global, like emerging market debt which has very attractive properties. But my sense is as much as we're kind of thinking about or it's nice to read about stories of how people will be driving in to work and what kind of investment opportunities come from that, BMO's striking investment implication of what happens from COVID is we are re-entering the next chapter of search for yield and that will be incredibly disruptive to the industry in my view. And the second, I call it a second wave, maybe that term is going to be used so much that the second wave of low interest rates that maybe even eventually [INAUDIBLE 00:24:03]. So I'm going to stop here because that's my time. I hope that I've given you a framework to think here. My main takeaway for you is as we hear about information, we really try to buck it in one of these three phases and if we can get the timelines right, I think that we can make even better investment decisions along the way. And with that, I will pass it back to Glen. Thank you for your time and thanks for dialing in today.

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

Thank you very much, Francis. I'm probably one of the few people during the COVID crisis that has no concern about hairdressers, so I'm not waiting for the rush back. Our next speaker, Jamie Robertson, is Senior Portfolio Manager and Senior Managing Director and the Head of the Asset Allocation team in Canada. He's also the Head of Global Tactical Asset Allocation for Manulife Investment 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 throughout Asia. This team is also responsible for developing the five-year asset-mixed forecast and models for the Manulife Private Wealth platform and is a key partner of Manulife Private Wealth. Based in Toronto, Jamie is responsible for overseeing all aspects of Manulife Canadian asset allocation franchise, including portfolio management, research and development, product development, business development and trading. I'm very pleased to welcome Jamie, who will put into context the short-term volatility we're currently experiencing and the impact it's having on investors' long-term saving goals. Jamie, over to you.

Jamie Robertson, Senior Portfolio Manager, Head of Asset Allocation, Manulife Investment Management

Thank you, Glen, and one of my tasks right now will be to share a screen, and I will apologize in advance for those who may not have a screen available, I'll try to frame my remarks for you to be able to follow along. But thank you, Glen, for inviting me today. I do appreciate the opportunity to chat with this group. You know Francis and I, as you mentioned, are part of a global team. We're actually the largest portfolio management team at Manulife. We manage over $140 billion in AUM and we are truly a global team. We have offices in Boston, Toronto, Montreal, London, and in Hong Kong. And the important thing to bear in mind is there's, you know, over 35 investment professionals, and really there's a sole dedication that they have, and that is to get up every morning and figure out where they can allocate capital to where it's going to be treated the best. So we build portfolios to have the highest risk-adjusted returns and that is our sole process. Thankfully, we've got, you know, Francis onboard, I mean to have an economist, a key strategist of her calibre to be able to have access to her on a daily basis, sometimes multiple times in the course of a day, is just a fantastic resource, and I think just speaks to how deep a team we have and how well resourced we are. But I was particularly pleased to have the opportunity to speak today about volatility and investing during periods of volatility, because I think it's one of the things that is probably not the best understood in the markets. So today what I'd like to do is I'd like to cover three aspects. Firstly is the high volatility often associated with risk, and I want to try to reframe that narrative a little bit. The second thing that I'd like to cover is what Glen referred to, which is the importance of an investment time horizon, timeframe, and why it is especially important during periods of volatility. And then finally, from your perspective, how can you take advantage of volatility and how can you seize that opportunity. So let's talk about the issue of volatility versus risk. Our industry equates volatility, or more specifically, the standard deviation returns as a measure of risk. So simply stated, if you look at two assets and one asset has a higher standard deviation of returns, generally people in our business would say that's risker. But by extension, an asset class that has seen a dramatic decline often virtually is guaranteed to have a higher standard deviation of returns suggesting higher risk. So just ponder on that a little bit. Our industry considers that an asset class that has fallen dramatically in price to be riskier. The lower the price, the higher the risk. Not exactly completely intuitive, but that's how our industry looks at it: Volatility is risk. Now risk based on a standard deviation just gives you some sort of insight into the range of possible outcomes that you might be looking at, but not actually what that outcome will be. That's where

Francis comes in, where she's going to help us figure out what that outcome is going to be. So for an asset class like equities, for instance, they have generally returned about 7% annualized over an extended period of time and they've done that with about 14% standard deviation of returns, so basically 7 out of 10 years will be within that bound, and that bound will be either -7 on a 12-year basis or maybe +21 on that basis. But the only insight or useful information that you can glean from that, from my perspective, is that if you're looking at your account balances and you're down 7% on a year, that's not a reason to panic any more than if you look at your account balances and they're up 21% is a reason to celebrate. But understanding the potential range of outcomes over a year does not really mean that much from a risk profile for investors. The risk that you and your advisor are managing is not volatility. It's not the short-term variability in your account balances from year to year. Your risks are very real and very different. Your first risk is a permanent loss of capital, and this will occur obviously when you sell an investment that has declined in value. You also have the risk of running out of money. You know this is something that our team spends a tremendous amount of time modelling for our group in retirement solutions shortfall probability, which is when you retire at 65, what are the chances that you will actually run out of money, and how do you build a portfolio to avoid that? Liquidity is another major risk, it's a real risk for investors. So not having cash on hand at the exact moment when you want it is a risk. You want to help a child with a down payment or a new baby, if you want to respond to an emergency, buy a cottage, buy a toy, if you don't have liquidity at that time, that's a risk that you run. Now achieving your portfolio objective is another risk. If you're thinking of 10, 15, 20 years or longer, you might be considering about your legacy or about the ability to do philanthropic work, and not achieving those objectives is a real risk. Overconcentration. Overconcentration can fit into all these other risks and that is simply having too much of your assets in one company or one commodity or one country, and that is just not a prudent way to manage your overall investment portfolio or your investment risk. And you've got reinvestment risk. So reinvestment risk is particularly pertinent to people who are in the position where they've got a lot of income or a lot of fixed income portfolios. As bonds mature that you may have bought 10 years ago yielding 6 or 7%, you know, you run the risk that you don't just have a compelling place to reinvest those funds and that is a real risk in terms of your long-term outlook. And finally, and this is something that you probably have not had to deal with for many, many years because inflation has been very stable and quite low, but you know, I got into the business 35 years ago so you might be able to guess how old I am, but at that point, inflation was a real problem and the problem with inflation is, in and of itself it is not necessarily an issue, but if you have investments that are not keeping up with inflation and beating inflation, then in fact you are suffering a decline in your real wealth. So those are the real risks that you face on an ongoing basis. So how do we sort of circle the square between what risk is and what volatility is as the way the market finds it and the way you think about it? So let's just do a little test here, again I apologize for those who don't have a screen, but I'm going to show you two asset classes. So here are two asset classes on the screen and they are quite different. There's one asset class, the blue line, that has actually over this time period has produced reasonably attractive returns. However, in the depths of despair it has had a minimum return of -38%. At the same time, it's had on the upside an exciting 63% on the upside, with a lot of wiggles along the way. So now we're looking at an alternative asset class, and this asset class over an extremely long period of time generates the same type of return, but it does so with much less volatility. Its worse return over this time period is a little bit less than -2% but on the other hand, its best performing period was a more pedestrian 22%. So which investment would you prefer of these two in the chart, and for those on the phone who can't see the chart, you know, an investment that has a variability of -38 to +63 or -2 to +22. Well to be honest with you, there's no wrong answer because really what you're looking at, these two investments are in fact one and the same. They are the TSX composite index. The first line, the blue line, is the one-year returns, and the red line is your five-year returns, and this is the collision between volatilities defined between standard deviations and the importance and impact of time horizon. Recall what I said earlier, with a 1-year time horizon, standard deviation of returns on equities mean that a normal year will have returns somewhere between -7 and +21, but with a 5-year time horizon, the standard deviation returns drops to basically 6 or 7%. So with an asset class that's returning 7 with a standard deviation of returns of 7, your range of outcome is basically sort of zero in one of the poorer periods of time to 14% on the upside. So I agree that you know, the long-term time horizon, and I would posit that most of the people on this call have a very long time horizon and it's an enormous investment and tax advantage. Buffet talks about this all the time. He will tell you that his number one strategic advantage in investing is an extraordinarily long time horizon. So how do you as an investor exploit that advantage along the lines of what Buffet does. Well, when volatility gets very extreme, it's an excellent time to basically do everything in your power to add to your investment portfolio. I'm showing a graph here that shows very definitive volatility regimes, and what you're seeing here is the rolling 100-day volatility of the TSX, and when you have extremely high levels of volatility such as we did in 1987, such as we did coming out of the aftermath of 2000 bubble, and in 2009 and today, what you get is, with very few exceptions, much more attractive returns on a one-year basis following a peak in volatility. You know the only time under which we've had underperformances than coming out of that 2000 period, but speaking of timeframe again, the more important thing is that once you've had a period of extremely high volatility, your five-year average return is well above average. It's anywhere from 150 to basically almost 500 basis points above average so that is a fantastic time for you to be able to take advantage of it. And the reason why the volatility is elevated is that it confirms the market adage that you often hear, and that is that the market climbs a wall of worry. It basically takes an escalator up but when it starts to head lower, it takes an elevator down and this is what causes all that volatility, all the headline risk and all the consternation in the market. But after these deep declines, volatility opportunity basically beckons. So how do we monetize on that, how do we take advantage of that? Well, we take advantage of that through our process. Our process forces us to take advantage of periods of short-term volatility. So the cornerstone of what we do is we build five-year expected return forecast for a vast majority of asset classes, and we do it with a five-year time horizon for a couple of reasons, one of which is we're building strategic asset allocation portfolios for our clients, and you should have a strategic asset allocation mindset. You should have a mindset that is at least five years in terms of your investments. And what our research has shown is that over a five-year period, that is the shortest period of time over which you can have what we refer to a normalization or a mean reversion in valuations. So if valuations are very, very expensive like they were in 1988, 1998 or 1999, you know it would have been a very poor time to invest in the markets because lo and behold, five years later, valuations had reverted back to the mean and it would have been a period of disappointing investment performance. On the other side when we think back to 2008–2009, valuations got to almost 45 or 50% below their long-term average, and of course what that meant was over the following five years out to 2014 what happened, valuations reverted back to the mean and actually got a little bit more expensive, so you had a massive, massive tailwind from valuations during that time period. So we do expect a return forecast, we do them for fixed income, we do them for equities, we do them for a number of private assets as well. On the fixed income side, it's pretty straightforward. We have an expression, you know, what you see is what you get, and that is that if you're starting off with yields around 1% in the investment grade space, that's kind of what you're going to get over that time period. Now of course you know, we're hunting around for yield, we're hunting around for better risk-adjusted returns, so we will wander into high yield, we'll wander to bank loans and to emerging market debt, but for the most part, you know the fixed-income area is a little bit more transparent in terms of what you can expect. Equity forecasting is a little bit different, and the way we think about equity forecasting is that we break it down into four components. So when you buy a stock, you know, what is going to define your return on that stock? Well, the first thing is you're going to expect to share in the profits of that company and you're going to get some income from it. You're going to get a dividend yield, and this is a very observable and for the most part quite stable source of income. The second thing that you want is you want some price appreciation, you want some growth, and our research has shown that in developed markets, nominal GDP is a pretty good proxy for price appreciation. So when you think about nominal GDP, what is that? Nominal GDP is real GDP, that's what you see in the headlines everyday plus the inflation. So right now, we're probably looking at nominal GDP over the next five years. For all intents and purposes, it's going to be about 2%, and inflation with some wiggles is probably going to be around 2% as well. And for those who can see it, you know the graph below shows that over time going back basically 75 years, that the SMP 500 actually does track nominal GDP quite closely. So that's what we think about in terms of price appreciation. The third part of it is valuations, so over the next five years, are you going to see valuation expansion and therefore a tailwind to returns, higher returns going forward, or are valuations expensive, in which case you can expect valuations to come down, annual returns are going to be more muted. And then the final thing that we take into consideration is, and I would highlight that our team in Boston spends much less time on this because all their portfolios are denominated in U.S. dollars, is that we have to take into consideration our view on currency adjustments. So we have to think about global investing from the perspective of a Canadian investor who is receiving those proceeds in Canadian dollars. So that is the cornerstone of how we start to build portfolios, and I'm sure that some of you who have seen this before, for those who can't, I'm showing the five-year expected return forecast for a number of asset classes. And again, I would highlight on the right-hand side, Canadian investment grade bonds, U.S. investment grade bonds, even global bonds, not a very compelling place to invest from a yield perspective. They do have diversification benefits, but they really are not going to move the dial in terms of generating the type of returns that I know that the people on this call require. As we said earlier, high-yield bonds and emerging market debt: slightly more interesting around 5 to 7% depending, and again, this is an area where the dynamics are very attractive but you are moving out the risk curve a little bit in terms of getting those types of returns. On the equity side, you know, we've got expected returns for Canadian large- and small-cap equities that are anywhere from 8.7 to 9.6%. The emerging market equity is another interesting area from our perspective, with returns over the next five years at 4.8%. U.S. large cap is the least attractive asset class going forward on the next five years. We expect the returns of somewhere around 4.8%. So for those of you who have never met me before or haven't heard me speak before, I would suspect you might have a certain level of concern about my credibility when I'm up here telling you that I can forecast expected returns for equity markets within 10 basis points for the next years, and I would agree with you. And I would also say that it's less important to us that we are absolutely precise in these expected return forecasts. What is more important to us is the ordinal rankings of them, how they get into a portfolio and what their relative ranking should be. So I don't know if U.S. large cap is going to be zero over the next five years. There are lots of asset allocation firms who believe it's going to be zero, and I don't know whether it's going to 4.8 or 8.8, but I do know that given growth dynamics, income dynamics and valuation dynamics, you know those are asset classes that are much more attractive on a relative basis going forward. So that's how we take advantage of short-term volatility by shifting our asset classes towards those asset classes that provide more attractive valuation and more attractive forward returns. We rely on our process, we use a long-term time horizon, and we allocate to more attractive assets. So what do you do to take advantage of these situations? Well to a large extent, you've already done it. You've already engaged an advisor and the data is absolutely crystal clear. Investors who use an advisor have much better outcomes in the long run than a do-it-yourself investor. The studies are clear, the anecdotal evidence is clear. The second thing you can do is certainly do not panic during these periods. Maintain that long, disciplined time horizon. That is one of your key advantages. Keep up with the plan that you have laid out with your advisor and increase to the extent if possible investments when you get into these periods when markets are extraordinarily weak. And basically, don't listen to the noise that you read in the press and hear on TV, but listen to your advisor. He's there to guide you through this. With the process that we have in place we can guide you through this and your advisor is ideally suited to help you achieve your investment objectives and to manage your risk. So thank you very much today and I hope you have a good day.

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

Jamie, thanks very much, that was great. Really good insight. It shows the importance of the long game and asset class diversification. The COVID-19 outbreak really threw financial markets off their projected course in the short term and has reshaped the economic and social landscape of the world. That said, as long-term investors who have navigated through many episodes of stress including the global financial crisis of 2007–2008, the European sovereign debt crisis, we know that this too shall eventually pass. Our managers are actively reviewing their portfolios and coupled with Manulife's Global Asset Allocation team, we continue to review our asset mixes based on long-term changes and risk profiles that we're seeing. We have seen some stability within the alternative asset classes, and we'll continue to monitor them for our client portfolios. We really hope today's comments were helpful to you. As always, if you're curious about what Manulife Private Wealth's investment platform can do for you and your clients, please don't hesitate to reach out to a member of the Manulife Private Wealth team. On behalf of the whole team and our other speakers, thank you for listening and we look forward to hosting our next call later this summer. Have a great day.

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