

# Wealth*Styles*

Asia-Pacific REITs:  
Yesterday's infant,  
tomorrow's grown-up

2019 Spring/Summer Edition



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## Editor's Note

Have you ever dreamt of landing a civil servant or public-institution job that will lead to a well-protected life without financial worries after retirement? For many people, having a stable income after retirement is a major concern. Nobody wants to see their pensions drained and their financial reserves depleted after they stop working, which is why people need to worry about overspending and a shortage of savings while they are still employed.

To solve the problem, it is crucial that everyone with sufficient investment capital is aware of the products they can use to help generate both personal and pension incomes. This includes people in the middle of their career or those nearing retirement. Take Real Estate Investment Trusts (REITs), for example. They are bound by law to distribute most of their earnings as dividends, providing a regular cash inflow for investors. Asia-Pacific REITs have consistently outperformed equities and property stocks in the kind of sideways interest-rate environment<sup>[1]</sup> we are currently experiencing. Not only that, they have a relatively low correlation with other asset classes<sup>[2]</sup>, making them an ideal tool for diversifying portfolios. In this issue's **Cover Story**, Hui Min Ng, Portfolio Manager (Equities) with 13 years' experience in Asia Pacific REITs, analyses the latest developments and investment potential of the region's REIT market.

Asian bonds are another good source of income. In **Fund Managers' Corner**, Fiona Cheung, Head of Credit Research, Asia and Jimond Wong, Senior Portfolio Manager, Fixed Income, reveal the secret recipe that's given them their winning edge, using a Michelin-starred restaurant as a metaphor.

Though there are various types of income products in the market, investors should be aware that risk and return are positively correlated. Blindly chasing high-yield investments while neglecting the sustainability of distribution and risks can do more harm than good. This issue's **Wealth Q&A** has more.

The message is simple; make the best use of your idle money and start investing as soon as possible. By evaluating risk and yield, it's possible to build a consistent income stream that will last a lifetime.

If you have any wealth management-related questions, we would like to hear from you. Email us at [WealthStyles\\_Asia@manulifeam.com](mailto:WealthStyles_Asia@manulifeam.com)

<sup>[1]</sup> Source: Bloomberg. Performance period: 31 December 2008 – 31 December 2015.

<sup>[2]</sup> Source: Morningstar, 31 December 2018.

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## The perfect income partner – *high yield with stable and regular distributions*

**Q** I am looking for a high-yielding product that offers stable and reliable payments. Can you help?

**A** “There is no best, only better” has become a philosophy of life for the modern generation. When seeking a life partner, some people yearn for a person who is amusing, wealthy and good looking. A good number of income investors may want the same, but from a financial perspective what they really desire is a product that offers a high yield with stable and regular distributions.

A recent survey by research group Cerulli asked asset and portfolio managers in six different markets, including Hong Kong and Singapore, to identify the most sought-after product features by Asian investors. The number one answer: regular and steady income payments.

It would, therefore, be safe to assume that among investment products with a similar risk profile in the same asset class, the one with a higher dividend would be the preferred choice.

However, don't forget that high yield comes at a price. Let's consider a high-yield multi-asset portfolio – it may be necessary to include investment instruments such as non-investment grade bonds, preferred stocks, convertible

bonds or even options to achieve a high single-digit or even double-digit dividend yield. These tools are associated with higher risk and volatility, and the underlying assets in the portfolio are more likely to be affected by variables, which impact the income distribution amount and frequency.

Bear in mind that the risk and return elements of an investment product form a distinctive pair that rise and fall together – higher returns come with increased risk and vice versa.

Keep your expectations realistic – a high-octane portfolio may suit the temperament of some investors, but it may not be the ideal choice for you. A sensible approach is to take an all-round view and consider the appearance (yield and distribution frequency) as much as the inner qualities (asset quality and potential risks) of a product and make appropriate decisions that match your desired risk tolerance level.



For more wealth management related enquiries, please email  
**WealthStyles\_Asia@manulifeam.com**

<sup>(1)</sup> Source: Cerulli Asian Distribution Dynamics, 2018.

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## Asia-Pacific REITs: *Yesterday's infant, tomorrow's grown-up*

From their infancy early in the millennium, Asia-Pacific (ex-Japan) REITs have grown steadily into an asset class worth more than US\$200 billion. As a relatively new asset class, AP REITs have weathered various storms in the last decade: the European sovereign debt crisis (2010/2011), US Federal Reserve's taper tantrum (2013), the China equities market meltdown (2014/2015) and US-China trade war concerns (2017/2018) and delivered steady returns with strong performance<sup>[1]</sup>.

In this issue of WealthStyles, Hui Min Ng, Portfolio Manager (Equities), shares her unique insights after 13 years of covering the market, and what the future potential of the asset class can offer investors at a time when investors are trying to figure out whether Goldilocks economy is back or economic recession is near.



**✿ You started your career as an analyst: how did this formative experience shape your current perspective as a fund manager for Asia-Pacific REITs?**

Previously, I worked as a sell-side analyst at a securities firm where the structure was very different from an asset management company.

For analysts at asset management firms, the emphasis is on broad sector coverage and keeping track of new companies in the investment universe. However, sell-side analysts have dedicated roles and responsibilities that require greater scrutiny of companies at a micro level.

During those years, I developed my analytical skills as I was able to conduct deep-dive analyses to understand the fundamental drivers of a company – primarily through building intricate financial models. Also, conducting bottom-up research helped test my assumptions in the model – not only for the equity side of the balance sheet, but also having a firm grasp on the liability side.

**✿ Back in 2006 when you started covering AP REITs, it was a relatively small investment universe (ex-Japan and Australia) with limited research resources. Did that help or hinder you?**

I was in an enviable position at the time, as I was able to cover the Asian REIT universe from what was effectively its infancy. In the major markets that we focus on, Singapore had its first REIT listing in 2002, followed by Hong Kong in 2005.

Back when that universe was smaller, it was easier to maintain coverage, and that enabled analysts and portfolio managers to get to know the management of REITs more closely.

Additionally, covering Asian REITs in the early stages provided first-hand experience and knowledge of each REIT's track record and ability to execute; not only of the REIT manager but of the sponsor (REIT parent company) as well.

**✿ You mentioned that knowing the management style of a REIT's parent company (or sponsor) is crucial. Why is that?**

Sponsors started spinning-off their projects and listing them as REITs in Asia in 2002. During those hectic years of intense IPO and listing activity, I witnessed so many different corporate dynamics and cultures among various sponsors, and that also helped me to understand the background of the REITs.



**Hui Min Ng**  
Portfolio Manager

These intellectual assets are crucial for my comprehension of the current and future expansion of REIT companies. It also means I'm able to predict more confidently whether a sponsor can turn around any failed projects, for example.

**✿ Online shopping and the broader digitalisation trend are affecting the traditional bricks-and-mortar retail model, which has implications for the occupancy rates of shopping malls. Recent technological developments may also impact the demand for office space in central business districts. To what extent do you see regional retail and office REITs being affected by digitalisation?**

Over the past three to five years, we have witnessed the impact of e-commerce on the traditional retail operating model.

When it comes to retail REITs, our focus has been twofold: 1) REITs that have a higher exposure to necessity malls as opposed to discretionary malls and 2) managers who have fortified their portfolio through reconstitution and asset-enhancement initiatives.

We have also concentrated on those retail REIT managers that have taken action to ensure that their assets provide not just an outlet for traditional retail, but have restructured existing assets to provide shopping "experiences".

When we talk about digitalisation, we are thinking about the new economy in which companies like Facebook, Google, and Amazon have been new creators of office demand. We view this as a positive development for office REITs that was not prevalent during the past 10 years.



Additionally, the broader digitalisation trend has resulted in the growth of data centres. Singapore's first pure-play data centre REIT was listed in December 2014, and we see industrial REITs in Singapore acquiring data centers located overseas.

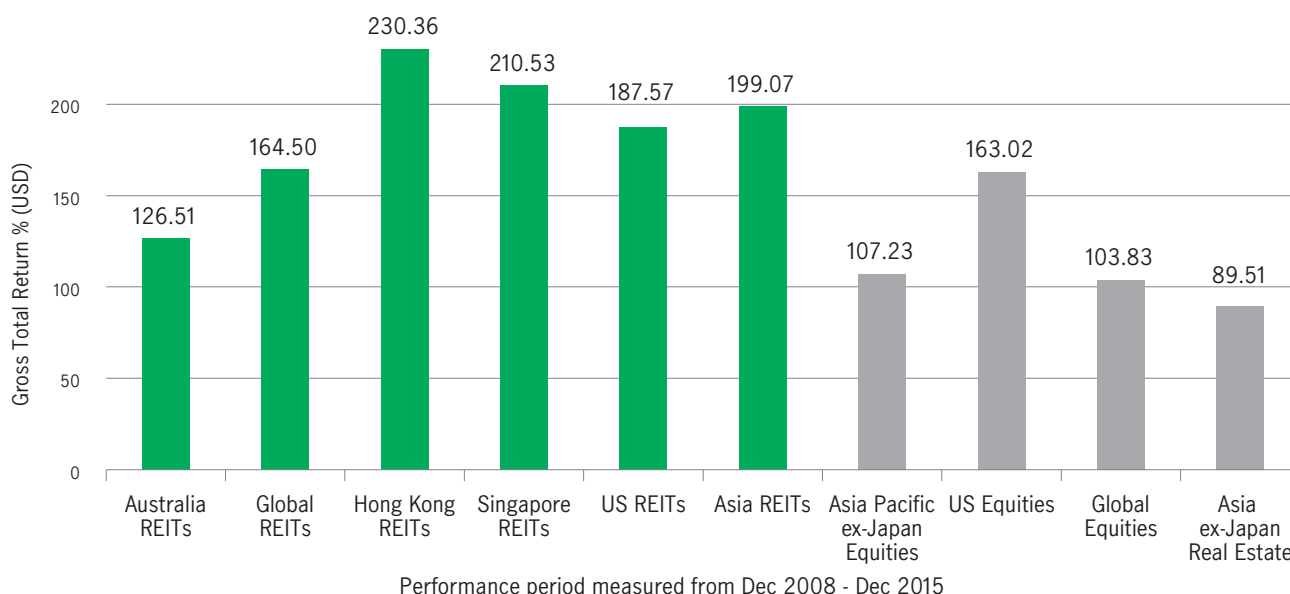
**✿ Rates have stabilised to the point where markets are expecting them to go sideways for a while. How do you expect AP REITs to perform in this environment, and will they outperform property developers?**

The last time the US experienced a sideways interest-rate environment was from December 2008 to December 2015. As you can see from Chart 1, most REITs have outperformed their broader equity counterparts, as well as property developers.

Also, REITs have improved their balance sheets over the last 10 years by reducing leverage, securing a higher percentage of fixed rate debt and extending their debt maturity profile. This has provided support to REIT valuations and enhanced their investment value.



**Chart 1: Most REITs outperformed equities in a sideways interest-rate environment**



Source: Bloomberg, gross total returns in US dollar. Performance period: 31 December 2008 - 31 December 2015. Australia REITs are represented by S&P/ASX 200 A-REIT Index. Global REITs are represented by S&P Global REIT USD Index. Hong Kong REITs are represented by Hang Seng REIT Index. Singapore REITs are represented by FTSE Straits Times REIT Index. US REITs are represented by MSCI US REIT Gross Total Return Index. Asia REITs are represented by FTSE EPRA/ NAREIT Asia ex-Japan REITs Index. Asia ex-Japan equities are represented by MSCI Daily Total Return Gross AC Asia Pacific ex-Japan USD Index. US equities are represented by S&P 500 Total Return Index. Global equities are represented by MSCI ACWI Net Total Return Index. Asia ex-Japan Real Estate is represented by MSCI AC Asia ex-Japan Real Estate Index, which also includes REIT exposure. Past performance is not indicative of future performance.

## The ABCs of Asia-Pacific REITs

### 1 How many different types of properties are covered by REITs in the region? Which ones offer the most significant potential, and why?

The Asia ex-Japan REITs universe offers a diversified mix of assets within the REIT space, as Chart 2 shows.

Within the universe, we are currently positive on office REITs in Singapore, Hong Kong, and Australia, given there's a supply-demand imbalance that will not be resolved until 2020/21. With high occupancy rates and continued demand for grade-A office space, we believe that high-quality office REITs should continue to see higher rental rates than previous leases (positive rental reversions).

Additionally, retail REITs in Singapore and Hong Kong have shown improving operating metrics as positive rental reversions continue.

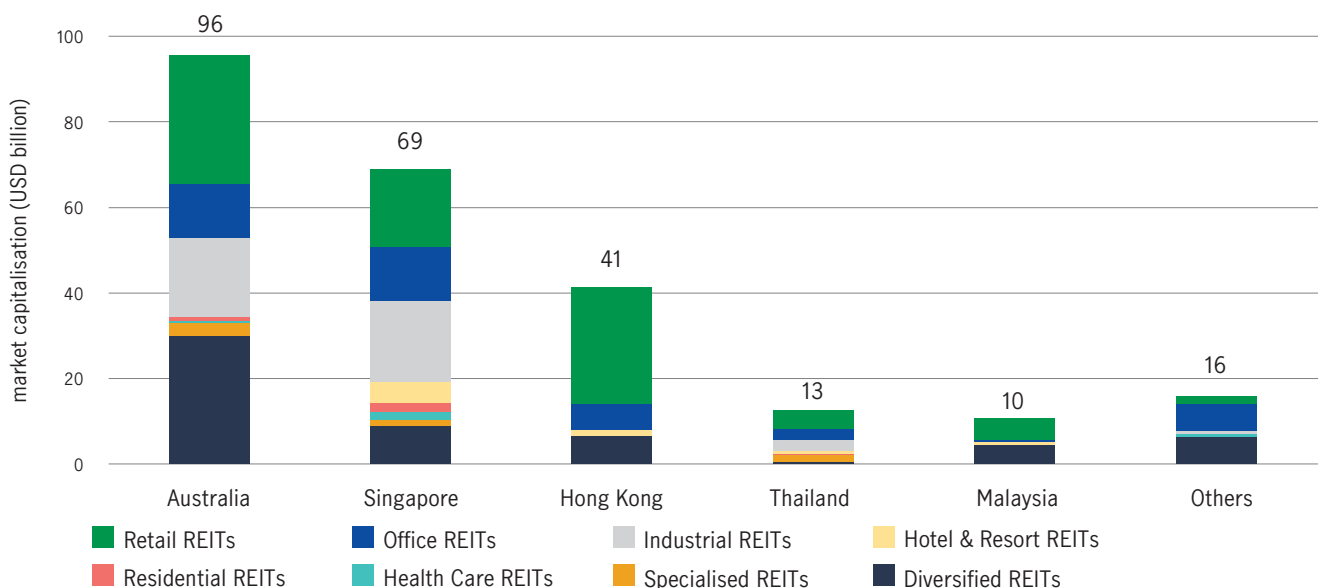
### 2 What are the key differences between investing in REITs and buying the shares of property developers?

REITs offer a steady and consistent income stream which is backed by longer term leases which results in REITs being more defensive relative to equities. However, REITs also offer capital appreciation potential which is driven by, but not limited to, rental income growth. REITs also offer exposure to many different types of properties.

For the most part, property developers' profits are reinvested into new projects, while REITs are bound by law to own income-producing assets and distribute their earnings to investors as dividends. In addition, there are limits on REITs' involvement in development projects. Because of these different operating models, the risk profiles are very different between the two.

Property developers' dependence on the macro cycle is much higher, given that they need to buy land, develop properties and sell assets to generate earnings continually. REITs operate on a different model and their income streams come from lease terms that are typically locked in (typically for three to seven years), and the expiry of those leases is usually staggered, so they provide visibility and stability to shareholders.

**Chart 2: Asia ex-Japan REITs Universe: US\$245 billion market capitalisation**



Source: Bloomberg, data as of 31 March 2019.

<sup>[1]</sup> Source: Bloomberg as of 31 December 2018. AP REITs are represented by FTSE EPRA/NAREIT Asia ex-Japan REITs 10% Capped Total Return Index. AP REITs generated total return of 15.7% p.a. (Price return: 9.8% p.a. + Dividend income: 5.9% p.a.).

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# Digitalisation – the *job* *opportunities* and *financial* *implications*

Everyone knows digitalisation is transforming the world as we know it, not only in terms of technology, but also in how people connect.

People communicate via social media and instant communication apps instead of letters. Today's newest internet celebrities interact with live viewers in chat on livestreams. Digital connectivity also redefines the “workplace” as it connects providers, customers and even competitors in new ways. But the key questions remain: which trends will dominate, and what do all they mean for planning your finances?

In the previous issue, we cited the latest Manulife Investor Sentiment Index (MISI) survey as we provided a brief regional overview of “digital readiness”. Emerging Southeast Asian markets and China were shown to be more sensitive to digital transformation (in terms of both risks and opportunities) compared to the relatively mature markets of Hong Kong, Singapore and Taiwan.

## The most popular types of digitally-enabled work

Regardless of age groups and markets, most respondents had online retail or digital-related part-time jobs (e.g. translation, web page development) as the main area of focus currently working in “digitally-enabled” roles. This was followed by online content creation (including video) and/or being an online influencer (with income generated via viewership revenue or sponsorship commission).

A smaller group of respondents got themselves involved in e-sports or app development jobs, either as gamers to win tournaments or create start-up companies of their own to develop new apps or technologies.





## Types of digitally-enabled jobs currently worked on

Market	Sell things or services on digital/online platforms	Digital-related online part time job or project	Online content creation/online influencer	E-sports/new apps development business
Thailand	66%	51%	18%-28%	10%-12%
Indonesia	62%	52%	21%-31%	16%-18%
Malaysia	59%	65%	17%-29%	14%
Taiwan	53%	55%	11%-35%	2%-6%
Philippines	52%	64%	14%-23%	10%-15%
Hong Kong	52%	43%	17%-30%	7%-11%
Singapore	47%	43%	22%-24%	8%-11%
China	42%	67%	14%-34%	5%-6%

Respondents could make multiple responses.

Source: Manulife Investor Sentiment Index Survey, second quarter of 2018

## Aspirations: As an income supplement

In addition to surveying current digitally-enabled workers, we also surveyed potential ones – people who expressed some interest in joining the digitally-enabled workforce but haven't joined yet. Overall, the trend reflected existing digitally-enabled worker career choices, except there was a higher percentage of respondents who aspired to work on their own tech start-ups or apps.

As for motivations, most respondents across all markets cited a desire to earn more income as the primary reason for working in digitally enabled jobs. This was then followed by a variety of career goal reasons (e.g. job satisfaction, flexible working hours, or exploration of new paths).

## The financial implications of doing digitally-enabled jobs

The main concern is obvious – part-time work and less stable forms of income generation (e.g. content creation, being an online influencer, online retail) looks to be on the rise. Many of these new digitally-enabled jobs are “high risk high reward”, and generally do not guarantee any hourly

income at all. Online influencers need an actively engaged fanbase; e-sports competitors need to win or perform well to stay on sponsored teams; tech start-ups and online retail platforms need large customer bases to support the business. If you're transitioning to these careers, it's best to do so out of interest or self-satisfaction first – do not count on digital part-time jobs necessarily being able to supplement your income.

### This points to a clear need for:

- Different saving strategies to prepare for retirement as workers transitioning away from traditional full-time jobs lose their protection.
- More advice on investment discipline and how to reinvest income appropriately amid less stable job income.
- Increased insurance protection for the self-employed.

The trend towards digitalisation – especially in emerging markets – provides with it many opportunities for further income generation and, in many cases, freedom in terms of work hours or location. But with that change comes a need to realise that now, more than ever, is the right time reassess one's own financial situation to ensure adequate protection from financial instability.

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## Asian Bond Team's Winning Edge



**Jimond Wong**

Senior Portfolio Manager,  
Fixed Income

**Endre Pedersen**

Chief Investment Officer,  
Fixed Income, Asia (ex-Japan)

**Fiona Cheung**

Head of Credit Research,  
Asia

### Proprietary Credit Research: *Asian Bond Team's Winning Edge*

In a Michelin-starred restaurant, it takes more than just the skill of each individual chef, but also seamless teamwork, to produce the finest dishes.

Likewise, in producing a top-performing Asian bond strategy, the experience and expertise of each team member is as important as the bond between them.

We speak to the tag team – Fiona Cheung, Head of Credit Research, Asia of Manulife Asset Management (MAM) and Jimond Wong, Senior Fixed Income Portfolio Manager – to uncover the secret recipe behind their winning edge. Over the past ten years, Fiona has been leading the team of credit analysts across Asia, while Jimond, who joined MAM six years ago with experience in a full spectrum of credit investment, manages the Asian bond portfolio.



Fiona



Jimond

#### Tell us more about your backgrounds



Prior to joining MAM, I worked in various roles across the capital market value chain, from a traditional bank like Sumitomo Bank, credit rating agency Moody's, to a multinational financial institution like Morgan Stanley. Over the last 20 years, apart from gaining valuable experience, I have witnessed the development of the Asia credit market and the different market cycles.



My diverse experience in the credit analysis space, having conducted research across the credit spectrum, from investment grade to high yield and distressed bonds, has given me a unique perspective on Asian credit. I have witnessed the ups and downs of credits in diverse market environments, including the liquidation of one of China's largest state-owned companies, GITIC. It was an eye opener to witness such a big bankruptcy so unexpectedly back then, and the incident had inspired me to develop a career in credit research.

### What is unique about MAM's Asian credit team?

**F** In a primarily male-dominated asset management industry, MAM's Asian credit team is fairly well-balanced. The mix of male/female credit analyst is around 60/40.

We have an extensive local footprint. Our analysts in Hong Kong, China, Japan, Korea, Singapore, Malaysia and Indonesia read and speak the languages. This cultural diversity provides MAM with unparalleled access to local knowledge and intelligence.

### Has the credit research team ever made a bad recommendation?

**F** Throughout my 10-year career with MAM, we have never experienced defaults. We have also successfully avoided all 49 "Fallen Angels" (credit names being downgraded to non-investment grade). This is a strong testament to our robust credit process.

### Did the team suffer losses as a result of the various China USD bond market defaults in 2018, or experience disappointments with issue selection?

**J** We have avoided all defaults and this has underscored our strong performance over the past couple of years.

Our selections are made after robust discussions with the credit team. By leveraging the expertise of our credit analysts, using their inputs intelligently and managing our risks correctly, we have consistently generated alpha in our investment process.

### As the process is binary, are there internal challenges to your credit calls?

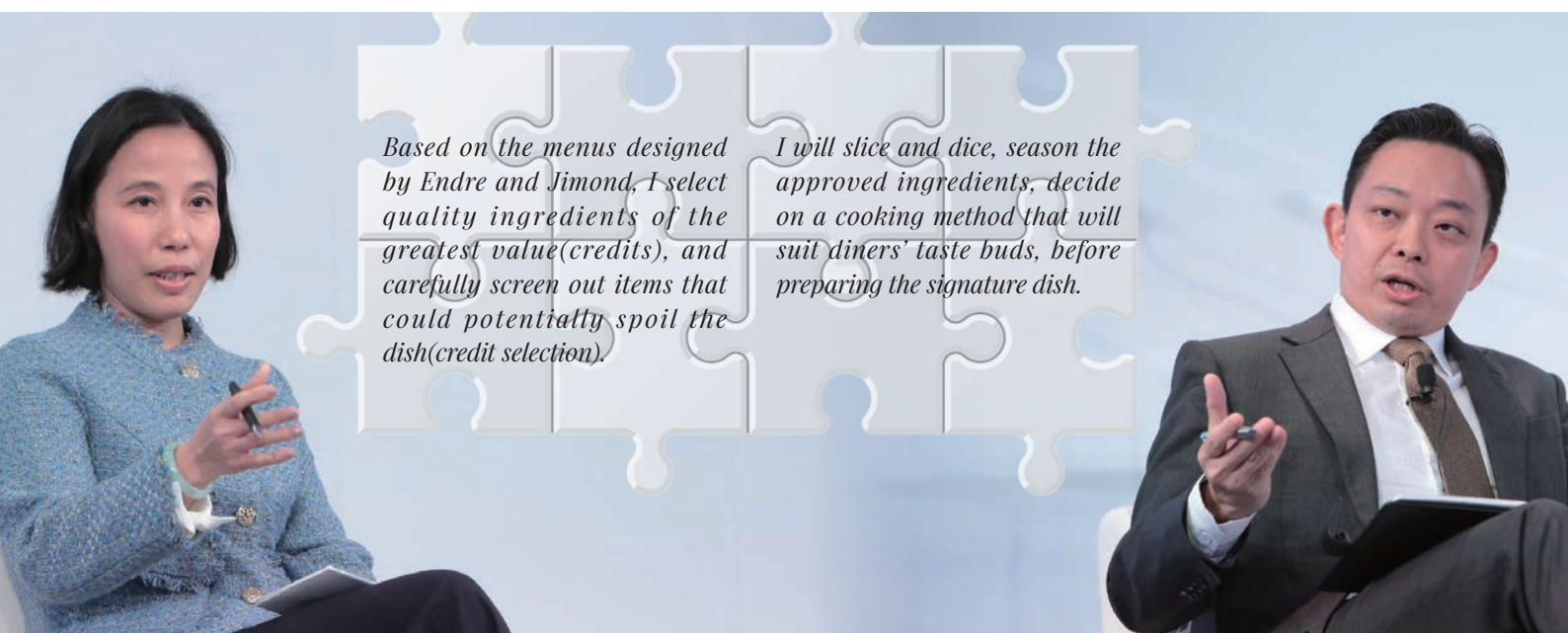
**F** Our job is to limit any potential downside by sifting out the "bad apples" or questionable names from the investable universe after a stringent screening and security selection process.

Equally important is helping our portfolio managers generate new investment ideas by identifying relative value trades, mispriced names, market dislocations, or going down the bank capital structure and identifying upgrade/downgrade candidates ahead of the rating agencies and the market. To achieve this, it is crucial to have a large, strong and cohesive credit research team.

### How do you maximise teamwork?

**F** Using a Michelin-starred fine-dining gourmet restaurant as a metaphor: Endre Pedersen, our Asia Fixed Income Chief Investment Officer, is the Head Chef who has assigned his two Sous Chefs, Jimond and I, with different duties. Based on the menus designed by Endre and Jimond, I select quality ingredients of the greatest value (credits), and carefully screen out items that could potentially spoil the dish (credit selection).

**J** Akin to portfolio construction and bond selection, I will slice and dice, season the approved ingredients, decide on a cooking method that will suit diners' taste buds, before preparing the signature dish.



*Based on the menus designed by Endre and Jimond, I select quality ingredients of the greatest value(credits), and carefully screen out items that could potentially spoil the dish(credit selection).*

*I will slice and dice, season the approved ingredients, decide on a cooking method that will suit diners' taste buds, before preparing the signature dish.*

**F** Strong teamwork, trust, communication and collaboration are crucial. The core team, including Endre, Neal (Senior Portfolio Manager, Fixed Income) and Jimond, has been working together for over seven years and there is a high level of rapport which is invaluable.

**J** As a portfolio manager from an accounting and analyst background, I speak the same lingo as our credit analysts, and they are comfortable working with me. Whenever the analysts spot anything, they simply look for me or call me for a quick chat. We coordinate actions across our portfolios, after taking into account factors such as market technical and macro trends.

### What have you learned from your exposure to the different research processes in credit-rating agency and a fund house?

**F** Proprietary credit research is the key to unlocking investment opportunities. Only invest in names which you have done sufficient homework. Regardless of a bullish or bearish market, we need to maintain level-headedness, and not be swayed by short-term hype or

distractions.

**J** In my view, rating agencies place consistency at a higher priority than a holistic portrait of creditors, relying on financial analysis and management presentations. On the flip side, they can also request information that are not available to the public, giving them a better gauge on the companies' financial and operating trends, which is equally important to credit analysis.

Our research team evaluates the agencies' actions and their related impact on the market. Many times, we are ahead of the rating agencies due to our proprietary research.

Fiona and Jimond participated in a lively discussion hosted by Michael Domermuth, Executive Vice President, Head of Wealth and Asset Management, Asia.



The trio successfully engaged the audience by detailing the Asian bond team's superior proprietary credit research capabilities and enviable track record to investors who attended the Regional Investment Conference held in Tokyo, February 2019.

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## 10 need-to-know facts about the *US bull market's 10<sup>th</sup> anniversary*

Whether you view the current bull market as being on its last legs or still having plenty of gas left, it's clearly demonstrated its stamina. 9 March 2019 marks the 10<sup>th</sup> anniversary since the US stock market sank to its financial crisis low point in 2009.

That decade-long run makes this the longest bull market in stock market history. It's achieved that distinction by maintaining upward momentum without suffering a 20% decline or more from a market peak. That threshold of a 20% move in the S&P 500 Index is the point at which a bull market turns into a bear market, or vice versa, by the most common method for defining each type of market.

While this bull hasn't been without setbacks and steep declines, its huge overall gains and the accompanying economic recovery have helped restore wealth lost in the financial crisis. Here are 10 key things to know about this bull market as it turns 10.



### **Already a record breaker**

The bull market didn't need to reach 10 years of age to break the length record. It achieved that distinction on 22 August 2018, when its duration exceeded a bull market that ran from October 1990 until March 2000, when the tech bubble burst.



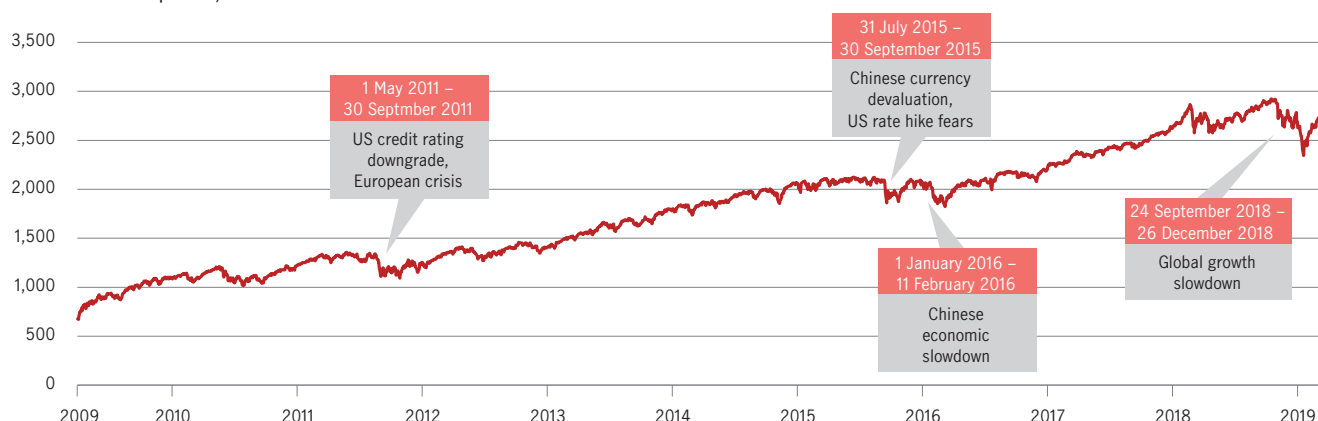
### **Near-death experience**

This bull's closest brush with an untimely demise came on 24 December 2018, when a three-month-long market decline sent the S&P 500 tumbling 19.8%. Two days later, stocks began a months-long rally, the bull stayed alive, and the bear went back into hibernation. (However, another major stock index, the NASDAQ Composite, did enter a bear market on 24 December 2018, as its decline from a recent peak exceeded 20.0%; it then proceeded to return to bull territory by rebounding more than 20.0% by mid-February 2019.)



## This bull market has had brushes with death, but it's still going strong at 10

S&P 500 Index prices, 6 March 2009 – 1 March 2019



Source: US Federal Reserve Bank of St. Louis, Bloomberg, 1 March 2019. The S&P 500 Index tracks the performance of 500 of the largest publicly traded companies in the United States. It is not possible to invest directly in an index. Past performance does not guarantee future results.



### Wealth builder

The rise in the S&P 500 during the bull market added US\$17.5 trillion to the index's total market capitalisation as of 5 March 2019, according to S&P Dow Jones Indices. Factor in gains from dividends, and the total rises to US\$20.8 trillion. That amounts to an average gain of over US\$63,000 in added wealth per person across the US.



### Attractive returns

The S&P 500 has gained 312.4% through 5 March 2019 on a price basis, while posting a total return of 408.4%, factoring in reinvested dividends.<sup>[1]</sup> On an annualised basis, the total return has averaged 17.7% – over two times the market's annualised return of 5.4% dating to the start of 2000, and almost double the 9.6% gain dating to 1990.<sup>[1]</sup>



### Sector leader

The top-performing S&P 500 sector during the bull market has been consumer discretionary, with a 596.2% price gain through 5 March 2019.<sup>[1]</sup> Information technology is second with 521.4%.



### Sector laggard

The worst-performing sector has been energy, with a 57.0% gain.<sup>[1]</sup>



### Small-cap outperformance

The Russell 2000 Index, a common benchmark of small-cap stock performance, has topped the large-cap S&P 500 during the bull market, with a 359.0% price gain.<sup>[2]</sup>



### Bond market performance

During this bull market's epic run, longer-term bond yields have gone essentially nowhere. The yield on 10-year US Treasuries on 9 March 2009, was 2.89%; a decade years later, it was around 2.70%. There was plenty of volatility along the way, as the 10-year yield hit a high of 4.01% on 5 April 2010, and a low of 1.37% on 5 July 2011. The US Federal Reserve (Fed) was one of the main reasons for this range-bound trend; through quantitative easing, the Fed purchased trillions of dollars of Treasury debt to help stimulate the stock market. Today, it's reversing that trend by rolling Treasury debt off its balance sheet.



### Gold's underperformance

While the S&P 500 powered to its 312.4% bull market gain, the price of an ounce of gold climbed just 41.8% over the same period.<sup>[3]</sup> Many investors buy gold as a hedge against inflation, which has remained muted through most of this bull market.



### Volatility's decline

The Cboe Volatility Index, which measures investors' expectations of short-term equity market volatility, stood at 49.7 when the bull market started.<sup>[4]</sup> As of 5 March 2019, it was just 15.2, close to its historical average.

<sup>[1]</sup> S&P Dow Jones Indices, March 2019.

<sup>[2]</sup> Bloomberg, 9 March 2009 – 5 March 2019.

<sup>[3]</sup> <https://www.macrotrends.net>, 1 March 2019.

<sup>[4]</sup> <https://finance.yahoo.com>, 1 March 2019.

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## How a *rate-hike pause* affects you

The US Federal Reserve (Fed) paused its rate-hiking cycle in January 2019. This position was maintained at subsequent policy meetings, and the majority of officials now expect only one more rate increase over the next two years, with some even discussing the circumstances that may warrant rate cuts. Under “normal” conditions, such a hiatus would be interpreted by investors as a risk-on signal, so it raises the question: will this move be positive or negative for investment markets?

Perhaps the answer can be found by looking at trends in US equities and various asset classes following the past three rate-rising cycles.<sup>[1]</sup>

### Scenario 1

Rate-hike cycle:  
30 June 1999 – 16 May 2000

S&P 500 Index	The index peaked about three months after the last rate hike <sup>[2]</sup> The index rose by 3.73% during the period
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#### Asset performance in the same period before US equities peaked

US bonds <sup>[5]</sup>	+5.82%
Asian bonds <sup>[6]</sup>	Local-currency bonds: no reference information Corporate bonds: no reference information
Asia-Pacific REITs <sup>[7]</sup>	No reference information
Australian dollar	-0.03%
New Zealand dollar	-8.97%
Japanese yen	+2.60%
US dollar index	+0.10%

### Scenario 2

Rate-hike cycle:  
30 June 2004 – 29 June 2006

S&P 500 Index	The index peaked about 15 months after the last rate hike <sup>[3]</sup> The index rose by 23% during the period
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#### Asset performance in the same period before US equities peaked

US bonds <sup>[5]</sup>	+9.43%
Asian bonds <sup>[6]</sup>	Local-currency bonds: no reference information Corporate bonds: +12.45%
Asia-Pacific REITs <sup>[7]</sup>	No reference information
Australian dollar	+21.90%
New Zealand dollar	+26.67%
Japanese yen	-1.66%
US dollar index	-8.61%

### Scenario 3

Rate-hike cycle:  
17 December 2015 – 20 December 2018

S&P 500 Index	No clues yet as to when the index will peak The index rose by 19.39% <sup>[4]</sup> during the period from the last rate hike to April this year
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#### Asset performance since the last rate hike

US bonds <sup>[5]</sup>	+3.68%
Asian bonds <sup>[6]</sup>	Local-currency bonds: +2.68% Corporate bonds: +5.86%
Asia-Pacific REITs <sup>[7]</sup>	+12.67%
Australian dollar	-0.84%
New Zealand dollar	-1.49%
Japanese yen	-0.13%
US dollar index	+1.25%

## Risk assets

US equities – Historical data for the period covering the past three rate-hike cycles shows that equities did not immediately peak after the final rate increase of the sequence, but experienced a period of positive returns, as the more accommodative monetary environment helped to boost risk assets in the short term. However, investors must beware that the equity market would reach a high point then start to decline in a volatile trend, as concerns emerged about slowing growth and a potential recession.

An impressive display by equities does not imply good returns among other risk assets. Some non-US dollar risk assets, such as major foreign currencies (including the euro, sterling, the Australian dollar and the New Zealand dollar), posted mixed performances following the past three rate-hike cycles. The Australian dollar and New Zealand dollar, for example, rose more than 20% versus the US dollar under Scenario 2 but depreciated in the other scenarios.

## Non-risk assets

Bonds – A pause in rate hikes is normally positive, as bond prices tend to stabilise (as an increase in interest rates usually leads to a fall in bond prices). Regarding Scenarios 1 and 2, US bonds not only showed sustained positive returns before US stocks peaked, but the prices of these bonds also continued to rise when US share prices were in decline, resulting in a more stable long-term trend than equities.

As for Asian fixed income, we can only refer to Scenario 2 as the relevant index was only launched after 2000. In this scenario, Asian corporate bonds still recorded solid gains, with prices rising steadily even after US equities peaked and fell back in October 2007.

The relevant index for other income assets, such as Asia-Pacific REITs, was launched in 2008, which means that Scenarios 1 and 2 cannot be used as reference points. Nonetheless, Asia-Pacific REITs gained over 12% as of April 2019 following the Fed's recent pause to its rate-hikes.

The US dollar did not weaken decidedly after the end of the

cycle. The US Dollar Index, which reflects how it performs against a basket of major foreign currencies, recorded moderate gains in Scenarios 1 and 3. However, safe-haven currencies, such as the yen and the Swiss franc, are not necessarily correlated with the US dollar. Case in point: In Scenario 2, the US dollar fell by more than 1% against the yen, but the Swiss franc rose close to 5% against the dollar, amid a decline of more than 8% in the US dollar.

## Conclusion

Investors should note that the influence of US interest rates is not limited to the domestic market, but can spill over to the global investment markets through the US dollar – the so-called "ripple effect". Therefore, it would be wise to consider a balanced approach to allocation: risk assets can be supported by benign monetary policies, whereas fixed-income products add to the defensiveness of a portfolio, especially in late economic cycle. Meanwhile, income assets provide both offensive and defensive qualities. Investors are advised to regularly review their asset allocation and target investment-time horizon, as no single strategy is suitable for all situations.

### Did you know?

In 2019, the financial media is reporting the rhetoric of central banks as "turning dovish" or claiming that central banks are making "dovish shifts". What do these phrases mean? "Dovish" people or organisations are those that advocate moderation, while the opposite are those with a "hawkish" stance. With the Fed adopting a dovish stance this year, most officials are in favour of accommodative monetary policies. This has led to an easing of the Fed's monetary policies, as it looks to boost the economy by pausing interest-rate hikes or even cutting rates.

<sup>[1]</sup> Federal Reserve Open Market Committee: <https://www.federalreserve.gov/monetarypolicy/openmarket.htm>

<sup>[2]</sup> Bloomberg, the S&P 500 index peaked on 1 September, 2000. Index in USD terms.

<sup>[3]</sup> Bloomberg, the S&P 500 index peaked on 9 October, 2007. Index in USD terms.

<sup>[4]</sup> Bloomberg; as of 30 April, 2019.

<sup>[5]</sup> Bloomberg Barclays US Aggregate Total Value Unhedged USD Index.

<sup>[6]</sup> JP Morgan Asia Credit Index, iBoxx ALBI TRI Index.

<sup>[7]</sup> FTSE EPRA/NAREIT Asia ex Japan REITs Index.

Investment involves risk. Investors should not make investment decisions based on this material alone and should read the offering document for details, including the risk factors, charges and features of the product. Past performance is not indicative of future performance. This material has not been reviewed by the Securities and Futures Commission.