

Real assets can offer an income alternative to low bond yields

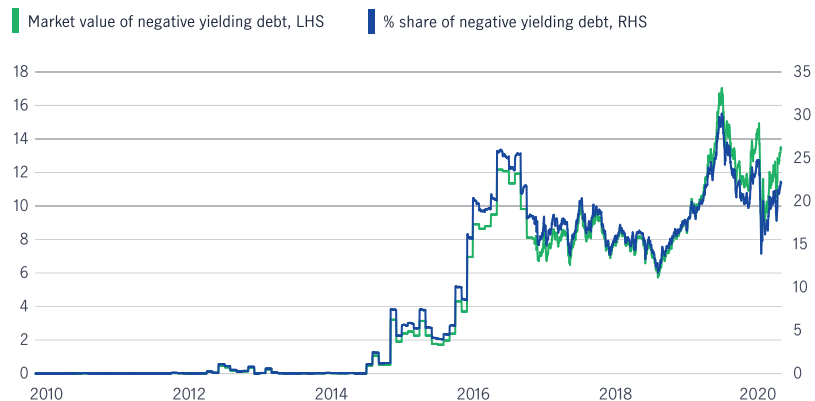
When it comes to seeking investment income, market participants typically turn to bonds. But alternative sources of income are becoming increasingly important as more investors discover that debt just doesn't yield enough to meet their portfolio distribution needs now. In working with clients around the world, we're seeing private real assets play a bigger role in generating robust investment income that's built to last.



Expected returns across global bond markets remain low

The 10-year U.S. Treasury note yields a nominal 0.5%, and that's about as good as it gets for high-quality government bonds these days: Comparable issues from Canada, yielding 0.4%, Japan, yielding 0.0%, and Germany, yielding negative 0.5%, appear even less likely to live up to their historical levels of income generation¹. In fact, our global chief economist expects major central banks to keep policy rates at or below zero until at least 2025, "a development that could push investors further out on the risk spectrum, swapping traditional government bonds for higher-yielding alternative assets."² If low bond yields have rendered portfolio distribution levels insufficient, then where might investors turn for income enhancement and stability? We see four distinct possibilities—and private real assets play a role in each case.

Share of global investment-grade bonds that are negatively yielding



Source: Macrobond, Bloomberg, as of June 18, 2020. LHS refers to left-hand side; RHS refers to right-hand side. The Bloomberg Barclays Global Aggregate Bond Index tracks the performance of global investment-grade debt in fixed-rate treasury, government-related, corporate, and securitized bond markets. It is not possible to invest directly in an index.

We favor private real assets generating robust, recurring cash yields

Private real assets include investments as diverse as airports, apartments, dams, farms, forests, and warehouses, yet they all share two defining features. First, they're not publicly traded, and therefore they offer the potential to earn an illiquidity premium over mainstream markets. Second, their intrinsic value is rooted in what's concrete, enduring, and essential, which, unlike more cyclical financial assets, tends to make real assets less vulnerable to unexpected changes in inflation, consumer preferences, and global growth. When chosen carefully, certain private real assets—real estate, timber, agriculture, and infrastructure—can also generate lots of income.

1 Real estate

Nimbleness has never been more important for real estate investors in search of attractive and stable sources of income. On the whole, structural shifts in commercial property appear to be helping industrial markets and hurting retail markets. While office markets represent an open question, the demand outlook for multi-family housing remains stable. Some segments remain better positioned than others, and we expect the global pandemic will alter the way people perceive, use, and invest in virtually all property types from this point forward. Real estate managers with narrow mandates and legacy assets might not be able to transact quickly enough to accommodate changing circumstances. Strategies with more flexibility could be better positioned to take advantage of shifting income streams on the horizon.

2 Timber

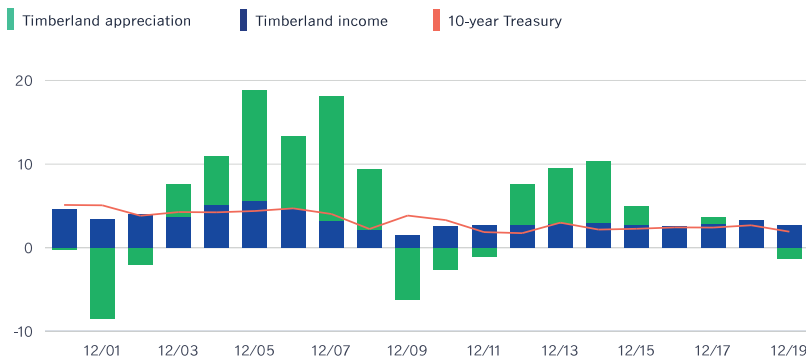
Timberland's long history of delivering competitive and consistent cash yields, inflation protection, and long-term capital appreciation has provided a strong incentive for investors to include the asset class in their portfolios. But timber's best days don't necessarily lie in the past. Today, the long-term outlook is no longer tied exclusively to revenues from the sale of unprocessed logs. The historical emphasis on commercial, production-oriented plantation forestry could broaden into new strategies focused on achieving the most cost-efficient capture and storage of carbon to meet the environmental goals of new tiers of capital focused on impact investment objectives. A growing and increasingly broader base of demand is likely to strengthen forest property values as voluntary carbon offsets continue to reshape the timberland market. Any rise in carbon prices may increase income opportunities for timber investors, a dynamic that might still be underappreciated by the market.

3 Agriculture

From a finite supply of arable land, the planet needs to nourish and sustain a global population that's already grown to 7.8 billion and is expected to reach 9.8 billion by 2050³. Recognizing the increasing challenge to feed the world, there's been growing investor interest in farmland for permanent crops—such as apples, pistachios, and wine grapes—and row crops—such as corn, potatoes, and soy beans. While many independent factors drive income returns for farmland, the relatively inelastic demand for food products keeps the industry comparatively insulated from downturns

Timberland has offered dependable cash yields, capital appreciation, and limited drawdowns

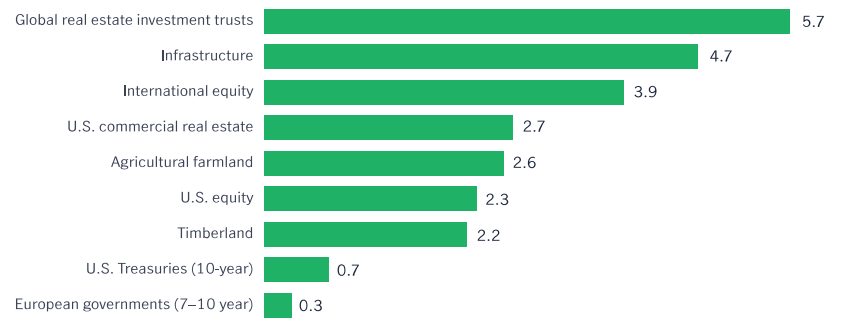
U.S. timberland and U.S. Treasury annualised returns (%)



Source: NCREIF, Macrobond, Hancock Natural Resource Group, December 2019.

Investors need to look beyond bonds for today's best yields

Yields (%) by asset class, March 31, 2020⁴



Source: Bloomberg, Hancock Natural Resource Group, J.P. Morgan Asset Management, March 31, 2020.

in the economic cycle. In fact, we've seen food purchases surge as people react to COVID-19 containment efforts by stockpiling their pantry shelves at home. Food and agriculture still function as defensive sectors, remaining less vulnerable to consumer spending curtailment than most goods and services.

4 Infrastructure

Infrastructure enterprises engaged in providing essential public goods and services — through electric, gas, and water networks; power-generation plants; transportation networks, including highways, railroads, and ports; and telecommunication towers — may benefit from limited competition and stable demand from consumers. While the capital appreciation component of infrastructure's total return can be volatile from one period to the next, long-term contracted cash flows, or regulated inflation adjusted rates of return, tend to underpin the income component, which has remained relatively stable over time. As the asset class continues to evolve and expand, network data centers, renewable energy, and other enduring assets tied to technological innovation are creating new income opportunities for infrastructure investors.

Diversified real assets can help build portfolio resilience

Relative to mainstream markets, allocating to any one type of private real asset may enhance a portfolio's yield profile while reducing its price volatility. Still, in our experience, real assets work best when they work together. But just gaining access to these categories can be challenging enough. Without the right partner, building a diversified portfolio of direct commercial real estate, infrastructure, farmland, and forest properties can be challenging for most investors. Even among the largest and most sophisti-

cated players, few have expertise across all the major private real asset sectors. Select outsourced chief investment officer (OCIO) programs now make it easier to have a one entry point into a globally diversified allocation across a variety of private real assets. As the next chapter in the search for yield begins, we believe it's time for alert income investors to boost both the level and longevity of portfolio income by lightening up on lower-yielding bonds—and leaning into a diversified allocation of private real assets.

Find out more
www.manulifeim.com/institutional



Eric Menzer, CFA, CAIA, AIF
Senior Portfolio Manager, Global Head of Pension and Fiduciary Solutions
Manulife Investment Management

Manulife Investment Management

FOOTNOTE

1 Wall Street Journal, YCharts, August 6, 2020.

2 "The three stages of the global economic recovery," Manulife Investment Management, July 24, 2020.

3 worldpopulationhistory.org/map/2020/mercator/1/0/25/, 2020.

4 Figures represent trailing 12-month cash yields as of March 31, 2020. Global real estate investment trusts represented by the FTSE EPRA/NAREIT Global Real Estate Index, which captures general trends in eligible real estate equities worldwide. Infrastructure represented by the MSCI World Infrastructure Index, which captures the global opportunity set of companies that are owners or operators of infrastructure assets. International equity is represented by the MSCI All Country World Index (ACWI) ex-U.S. Index, which tracks the performance of publicly traded large- and mid-cap stocks of companies in 22 developed markets and 23 emerging markets. U.S. commercial real estate is represented by the NCREIF Property Index (NPI). Agricultural farmland is represented by the NCREIF Farmland Index. U.S. equity represented by the MSCI USA Index, which tracks the performance of publicly traded large- and mid-cap stocks of the U.S. market. Timberland is represented by the NCREIF Timberland Property Index. U.S. Treasuries (10-year) represented by the 10-Year Treasury Constant Maturity Index, published by the U.S. Federal Reserve tracks the performance of a range of U.S. Treasuries, reflecting maturities that have been adjusted to the equivalent of a 10-year security. European governments (7-10 year) represented by the Bloomberg Barclays Euro Aggregate Treasury 7-10 Year Index. It is not possible to invest directly in an index.

Important Information A widespread health crisis such as a global pandemic could cause substantial market volatility, exchange trading suspensions and closures, and affect portfolio performance. For example, the novel coronavirus disease (COVID-19) has resulted in significant disruptions to global business activity. The impact of a health crisis and other epidemics and pandemics that may arise in the future, could affect the global economy in ways that cannot necessarily be foreseen at the present time. A health crisis may exacerbate other preexisting political, social, and economic risks. Any such impact could adversely affect the portfolio's performance, resulting in losses to your investment. Investing involves risks, including the potential loss of principal. Financial markets are volatile and can fluctuate significantly in response to company, industry, political, regulatory, market, or economic developments. These risks are magnified for investments made in emerging markets. Currency risk is the risk that fluctuations in exchange rates may adversely affect the value of a portfolio's investments. The information provided does not take into account the suitability, investment objectives, financial situation, or particular needs of any specific person. You should consider the suitability of any type of investment for your circumstances and, if necessary, seek professional advice. This material, intended for the exclusive use by the recipients who are allowable to receive this document under the applicable laws and regulations of the relevant jurisdictions, was produced by, and the opinions expressed are those of, Manulife Investment Management as of the date of this publication and are subject to change based on market and other conditions. The information and/or analysis contained in this material has been compiled or arrived at from sources believed to be reliable, but Manulife Investment Management does not make any representation as to their accuracy, correctness, usefulness, or completeness and does not accept liability for any loss arising from the use of the information and/or analysis contained. The information in this material may contain projections or other forward-looking statements regarding future events, targets, management discipline, or other expectations, and is only as current as the date indicated. The information in this document, including statements concerning financial market trends, are based on current market conditions, which will fluctuate and may be superseded by subsequent market events or for other reasons. Manulife Investment Management disclaims any responsibility to update such information. Neither Manulife Investment Management or its affiliates, nor any of their directors, officers, or employees shall assume any liability or responsibility for any direct or indirect loss or damage or any other consequence of any person acting or not acting in reliance on the information contained herein. All overviews and commentary are intended to be general in nature and for current interest. While helpful, these overviews are not substitute for professional tax, investment, or legal advice. Clients should seek professional advice for their particular situation. Neither Manulife, Manulife Investment Management, nor any of their affiliates or representatives is providing tax, investment, or legal advice. This material was prepared solely for informational purposes, does not constitute a recommendation, professional advice, an offer, or an invitation by or on behalf of Manulife Investment Management to any person to buy or sell any security or adopt any investment strategy, and is no indication of trading intent in any fund or account managed by Manulife Investment Management. No investment strategy or risk management technique can guarantee returns or eliminate risk in any market environment. Diversification or asset allocation does not guarantee a profit or protect against a loss in any market. Unless otherwise specified, all data is sourced from Manulife Investment Management. Past performance does not guarantee future results. Manulife Investment Management Manulife Investment Management is the global wealth and asset management segment of Manulife Financial Corporation. We draw on more than a century of financial stewardship to partner with clients across our institutional, retail, and retirement businesses globally. Our specialist approach to money management includes the highly differentiated strategies of our fixed-income, specialized equity, multi-asset solutions, and private markets teams, along with access to specialized, unaffiliated asset managers from around the world through our multimanager model. These materials have not been reviewed by and are not registered with any securities or other regulatory authority, and may, where appropriate, be distributed by the following Manulife entities in their respective jurisdictions. Additional information about Manulife Investment Management may be found at manulifeim.com/institutional. Australia: Hancock Natural Resource Group Australasia Pty Limited, Manulife Investment Management (Hong Kong) Limited. Brazil: Hancock Asset Management Brasil Ltda. Canada: Manulife Investment Management Limited, Manulife Investment Management Distributors Inc., Manulife Investment Management (North America) Limited, Manulife Investment Management Private Markets (Canada) Corp. China: Manulife Overseas Investment Fund Management (Shanghai) Limited Company. European Economic Area and United Kingdom: Manulife Investment Management (Europe) Ltd., which is authorized and regulated by the Financial Conduct Authority; Manulife Investment Management (Ireland) Ltd., which is authorized and regulated by the Central Bank of Ireland Hong Kong: Manulife Investment Management (Hong Kong) Limited. Indonesia: PT Manulife Aset Manajemen Indonesia. Japan: Manulife Investment Management (Japan) Limited. Malaysia: Manulife Investment Management (M) Berhad (formerly known as Manulife Asset Management Services Berhad) 200801033087 (834424-U). Philippines: Manulife Asset Management and Trust Corporation. Singapore: Manulife Investment Management (Singapore) Pte. Ltd. (Company Registration No. 200709952G). South Korea: Manulife Investment Management (Hong Kong) Limited. Switzerland: Manulife IM (Switzerland) LLC. Taiwan: Manulife Investment Management (Taiwan) Co. Ltd. United States: John Hancock Investment Management LLC, Manulife Investment Management (US) LLC, Manulife Investment Management Private Markets (US) LLC, and Hancock Natural Resource Group, Inc. Vietnam: Manulife Investment Fund Management (Vietnam) Company Limited. Manulife Investment Management, the Stylized M Design, and Manulife Investment Management & Stylized M Design are trademarks of The Manufacturers Life Insurance Company and are used by it, and by its affiliates, under license. 520101 © 2020 Manulife Investment Management. All rights reserved. Manulife Investment Management, the Stylized M Design, and Manulife Investment Management & Stylized M Design are trademarks of The Manufacturers Life Insurance Company and are used by it, and by its affiliates, under license. U.S. law governs the terms of use of the global section of the Manulife Investment Management website. Local law governs the terms of use of the regional sections of the website, each of which is intended to provide general information only about Manulife Investment Management's organization and capabilities. Investors may access this information by selecting a specific location through the site navigation. Persons outside a selected location are advised to seek independent advice relating to the use of the site, as they may be prohibited from receiving such information under the laws applicable to their place of citizenship, domicile, or residence. Please see our global legal terms for additional guidance. 197 Clarendon Street, Boston, MA 02116