WHITE PAPER

MARTIN CURRIE

ASIA PACIFIC REAL INCOME

MAY 2016 FOR PROFESSIONAL CLIENTS ONLY

Martin Currie Australia's Real Income strategy has, since inception in 2010, been successful in generating market-beating returns with less volatility than the broader equity market, and delivering an attractive and growing income stream to investors. This has been achieved by targeting listed real assets such as real estate, infrastructure and utilities in Australia.

This paper looks at the potential efficacy of implementing such a philosophy across the Asia Pacific ex Japan region, with the creation of the Martin Currie Asia Pacific Real Income strategy.

Executive summary

Deutsche Bank Hong Kong was commissioned to undertake an independent, quantitative analysis of the premise behind the Asia Pacific Real Income strategy. That is, that listed real assets in the Asia Pacific ex Japan region (both developed and emerging) can meet the needs of investors requiring an attractive and growing income stream, combined with a total return delivered with less volatility than the broader equity market.

Listed stocks were screened for membership of relevant industry grouping for real assets, minimum market cap and liquidity, attractive dividend yield, low price volatility, and low beta, over the past 15 years.

The analysis indicates:

- The Asia Pacific Real Income simulated portfolio was able to deliver not only better income, but also better growth, and a better total return with less volatility and lower drawdowns than the MSCI AC Asia Pacific ex Japan index over the back-test period.
- The simulated portfolio was also able to provide higher returns and lower volatility than sector specific indices.
- The lower risk/better return characteristics of the universe have been consistent over the period of the back test.
- As the size of the universe has increased over the years, the range of potential returns within the simulated portfolio could be further enhanced by stockpicking, as proven in the model portfolio and supported by the evidence of the Australia Real Income strategy since inception.

THE PHILOSOPHICAL PREMISE: REAL ASSETS

Real assets are the tangible building blocks of the economy that we use every day. These include listed property trusts (REITs), utilities and owners of other essential infrastructure. Assets include shopping centres, office buildings, tollways, airports, power grids, gas pipelines, power generators, and rail networks, etc.

We have found that real assets, with their essential ingredients of a large sunk capital base which drives cash flow, and low ongoing capital expenditure needs, means they are less exposed to the business cycle. Real asset demand is typically driven by population growth which is in turn reinforced by control of supply. With these unique characteristics they can naturally raise prices over time, thus providing protection against inflation.

The strategy focuses exclusively on listed securities, and this avoids the common problems that unlisted infrastructure or property funds face in terms of liquidity and pricing transparency. In addition, investing in a benchmark-unaware manner avoids the concentration issues encountered by some REIT or utility indices.

Due to their unique features, we believe that listed real assets are able to provide investors with

- An attractive yield
- A growing income stream
- Lower risk than equities (beta and business cycle)
- Higher returns and lower volatility than sector specific funds

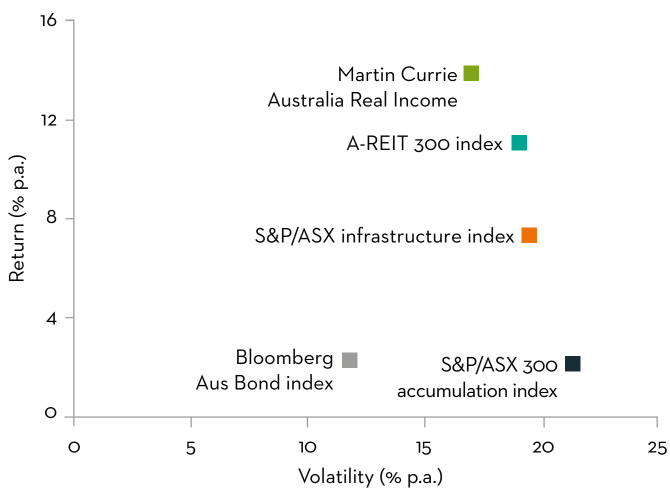
Through the use of further bottom-up, fundamental and quantitative research to focus the portfolio on the higher quality hard asset stocks, we believe that we can provide an even more attractive income stream.

As can be seen in the charts below, since inception, the Martin Currie Australia's Real Income strategy has delivered a dividend yield well in excess of the equity market, and has achieved its objectives of lower volatility, with returns far better than the broader equity market and sub-sectors.

Chart 1: Martin Currie Australia Real Income experience: higher returns for less risk

Dividend return (US$)

Total return and volatility (US$)



Past performance is not a guide to future returns.

Source: Martin Currie Australia, Factset; as at 31 March 2016. Based on a representative Australia Real Income portfolio in US$. The performance data is presented net of investment advisory fees, broker commissions and all other expenses borne by investors. The annual fee rate used is 0.75% plus expenses. Representative portfolio inception date: 1 December 2010. This strategy is not constrained by a benchmark but we show it versus the S&P/ASX 300 Accumulation index for illustrative purposes only.

The strategy is managed by the same investment team as Asia Pacific Real Income.

APPLICABILITY TO THE ASIA PACIFIC REGION

Through our experience of investing in Australian real assets, we believe that three of the key drivers of real asset returns – namely urban population growth, price growth and asset expansion – can also be applied to the broader Asia Pacific universe.

The Asia Pacific region is one of the fastest growing in the world. Its expanding population and rising incomes are leading to high levels of consumption and increased urbanisation, lifting demand for real assets such as infrastructure, real estate, utilities and essential services. As the population grows and demand increases in the short term, revenues should increase and lead to capital and income growth for investors. Additionally, most emerging Asian economies have underinvested in essential infrastructure, and there is a huge opportunity for global investors to participate in their funding. This growing and untapped inventory of listed assets offers significant investment opportunities in companies with stable characteristics and growing income streams. Often these are at more compelling valuations than their developed market counterparts.

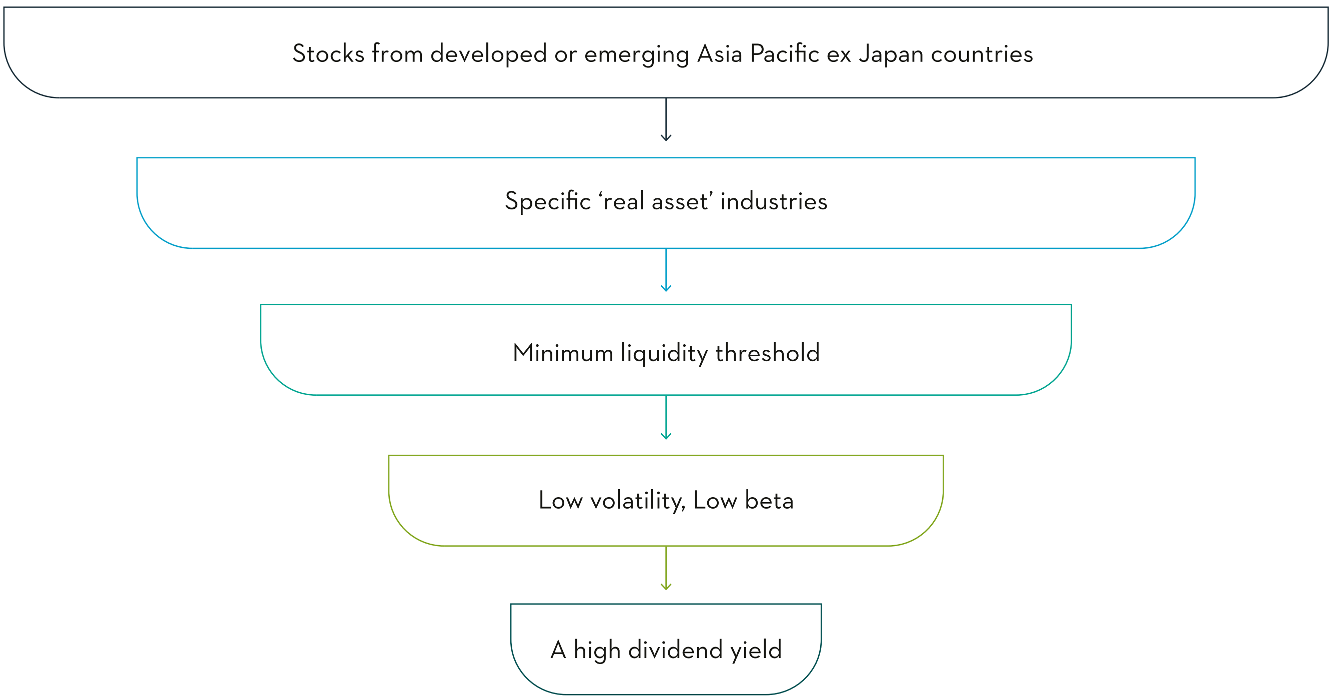
The Asia Pacific Real Income strategy aims to capture this opportunity by selecting existing brownfield real assets in both developed and emerging Asia Pacific countries that are leveraged to these key drivers.

THE PROOF

To support this research in an Asia Pacific Real Income strategy, Deutsche Bank Hong Kong was commissioned to undertake an independent, quantitative analysis of the premise. More specifically, they were asked to screen all stocks that that were listed on Asia Pacific ex Japan based stock exchanges in order to build a simulated portfolio.

The analysis period stretched over 15 years from September 2000 to August 2015. Data prior to 2000 was not used because until this point, there was not enough data for the testing to be meaningful.

The screen was for listed stocks that meet the following criteria:



More specifically, stocks from the following developed or emerging countries were included in the screen:

- Developed countries include Australia, New Zealand, Singapore, and Hong Kong
- Emerging countries include China, Malaysia, Thailand, India, Philippines, South Korea, Indonesia, and Taiwan

Due to the low risk focus of the strategy, it was determined that 'frontier' countries should not be included.

Regarding relevant industry inclusion, it was determined that the following industry groups (as classified by FactSet) were most representative of real assets:

- REITs
- Water utilities
- Electric utilities
- Gas distributors
- Oil & gas pipelines
- Railroads
- Other transportation
- Hotels/resorts/cruise lines
- Industrial conglomerates

As a minimum liquidity threshold, stocks with a low free float market cap and low daily liquidity were removed.

Reflecting the low risk focus on the portfolio, stocks with excessive price volatility or betas relative to their local MSCI index were removed. These were calculated using 12 months of daily returns.

Finally, reflecting the income focus of the portfolio, stocks with low expected dividend yields were removed.

Due to the regional nature of the stocks and the lag at which accounting data for stocks becomes public information for the corresponding time period, the analysis accounted for the relevant lags in a uniform manner across all stocks. Data was then cleansed by excluding abnormal observations at each month-end for the universe.

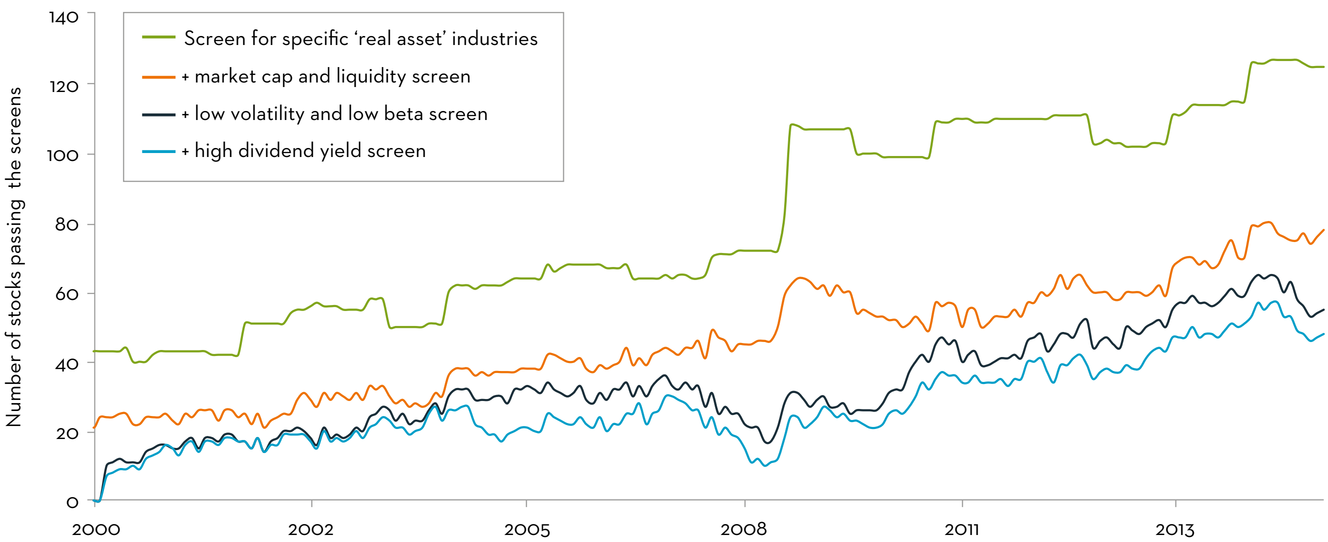
The screen was applied monthly. At this point stocks that passed the screen were rebalanced back to 1/n equal parts.

EXAMINING THE SIMULATED PORTFOLIO

The number of stocks passing the screen increased over the back-test period as shown in the chart below.

Chart 2: Number of stocks that pass the screen

For listed stocks in developed and emerging countries Asia Pacific ex Japan region



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Source: Deutsche Bank Hong Kong; for illustrative purposes only. Based on an un-audited simulated portfolio for 15 years to 31 August 2015 in US$. Simulated portfolio inception date: 1 September 2000. They were provided by Deutsche Bank Hong Kong and represent a back test of the strategy against using the screening criteria detailed in this paper.

In **pear,** investable stocks in Asia Pacific ex Japan countries in the specific 'real asset' industries

In **tangerine,** the sub-universe is then filtered for free float market cap and for liquidity

In **slate,** the sub-universe is subsequently filtered for volatility and beta

In **sky,** the sub-universe is subsequently filtered for dividend yield

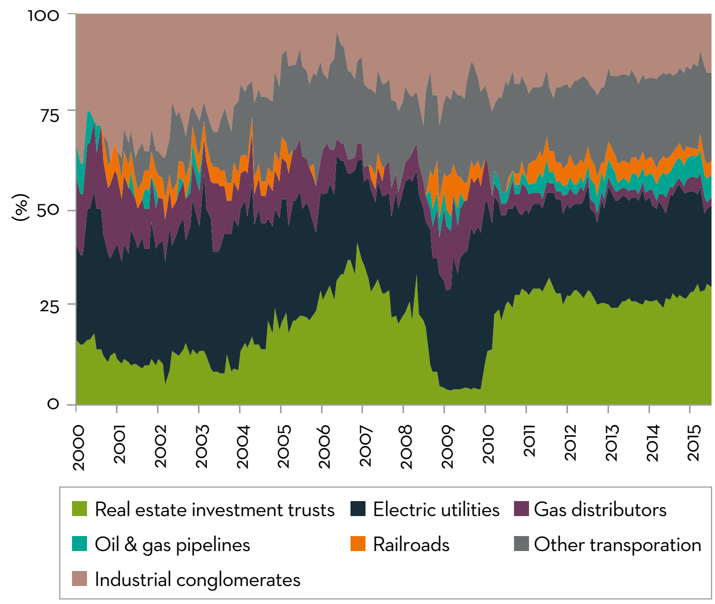
The increase in the number of real asset stocks in the universe through the period evidences one of the themes underpinning this strategy, being the continued investment and expansion of hard assets to meet the needs of a growing and urbanising population.

EXAMINING INDUSTRY AND REGIONAL EXPOSURES

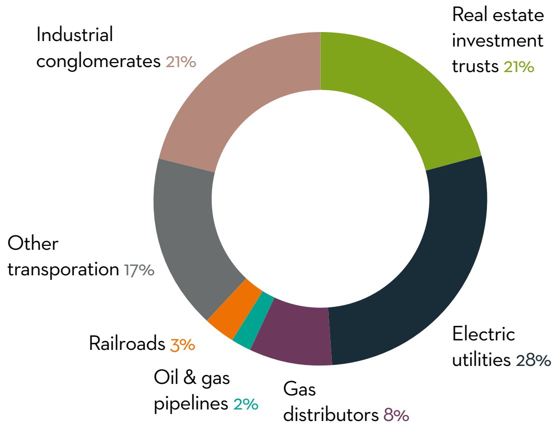
The results show a consistent breadth of exposure in stocks passing the screen by industry over the past 15 years, and outside of the period leading up to the global financial crisis (GFC) where REIT IPOs increased rapidly, and post-GFC where Australian REITS were compromised; there is no evidence that any back-test results are dominated by any single industry or country.

Chart 3: Breakdown of stocks that pass the screen by industry

Time series



Average



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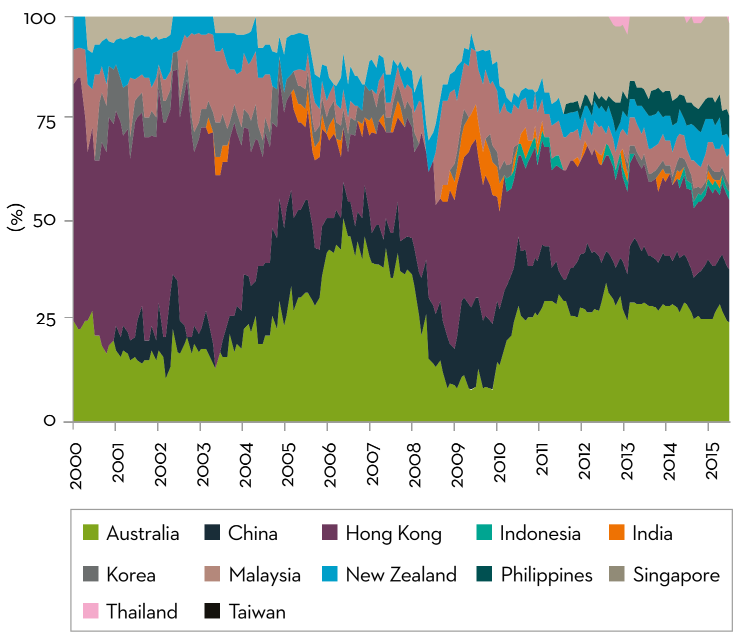
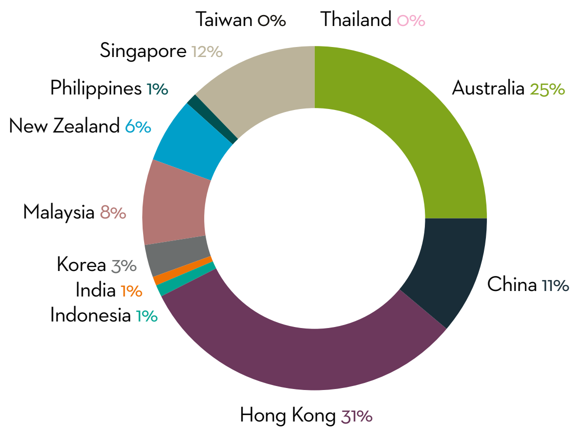
Similar analysis at the country level shows a wide spread of opportunity, which has stabilised post-GFC.

Chart 4: Breakdown of stocks that pass the screen by country

Time series



Average



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HISTORICAL PERFORMANCE AND BEHAVIOUR

Having identified the real asset companies that meet the screening criteria each month over the last 15 years, the next step was to analyse the returns that would have been achieved by investing in this universe. Both return and risk data were calculated on an equal weighted basis as described above.

The back-test results provided by Deutsche Bank show that, over the long term, the Asia Pacific Real Income simulated portfolio would have delivered not only better income, but also better growth, with a better return with less volatility and lower drawdowns than the broader market.

Summary results over the 15-year period versus the market and sub-sectors are given in the table and chart below. The market is presented by the MSCI AC Asia Pacific ex Japan index, and the returns for both market and the simulated portfolio include dividends. All returns are in US dollars.

Table 1: Asia Pacific Real Income simulated portfolio: summary results (US$)

	MSCI AC Asia Pacific ex Japan index	Asia Pacific Real Income simulated portfolio
Better income		
Delivered yield	3.1%	3.9%
Stronger growth		
Total return-delivered yield	4.5%	8.9%
Growth in forward income stream	6.8%	8.0%
Higher returns		
Total return (p.a.)	7.6%	12.8%
Alpha	0.0%	5.2%
Lower volatility		
Volatility (stdev p.a.)	21.1%	15.5%
Beta	1.00	0.65
Max drawdown	(60%)	(43%)
Months to recover	26	19
Up/down capture	100%/100%	76%/50%

Past performance is not a guide to future returns.

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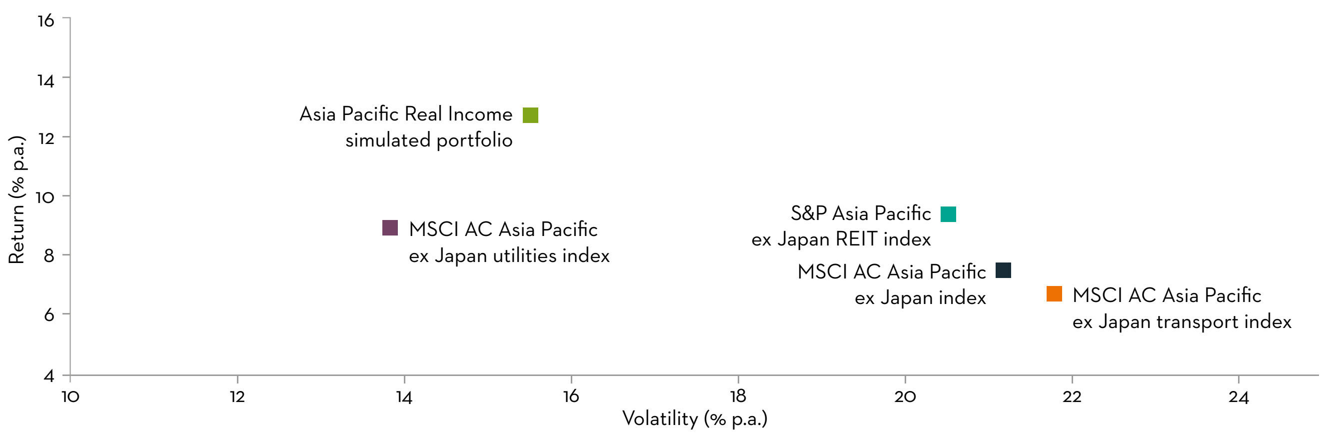
Source: Deutsche Bank Hong Kong; for illustrative purposes only. Based on an un-audited simulated portfolio for 15 years to 31 August 2015 in US$. The performance data is presented net of investment advisory fees, broker commissions and all other expenses borne by investors. The annual fee rate used is 0.75% plus expenses. Simulated portfolio inception date: 1 September 2000. They were provided by Deutsche Bank Hong Kong and represent a back test of the strategy against using the screening criteria which are detailed in the additional information at the back of this presentation. Theoretical results are shown without transaction costs that would reduce the return to investors. This strategy is not constrained by a benchmark but we show it versus the MSCI AC Asia Pacific ex Japan index for illustrative purposes only.

Chart 5: Asia Pacific Real Income simulated portfolio: total returns and volatility (US$)



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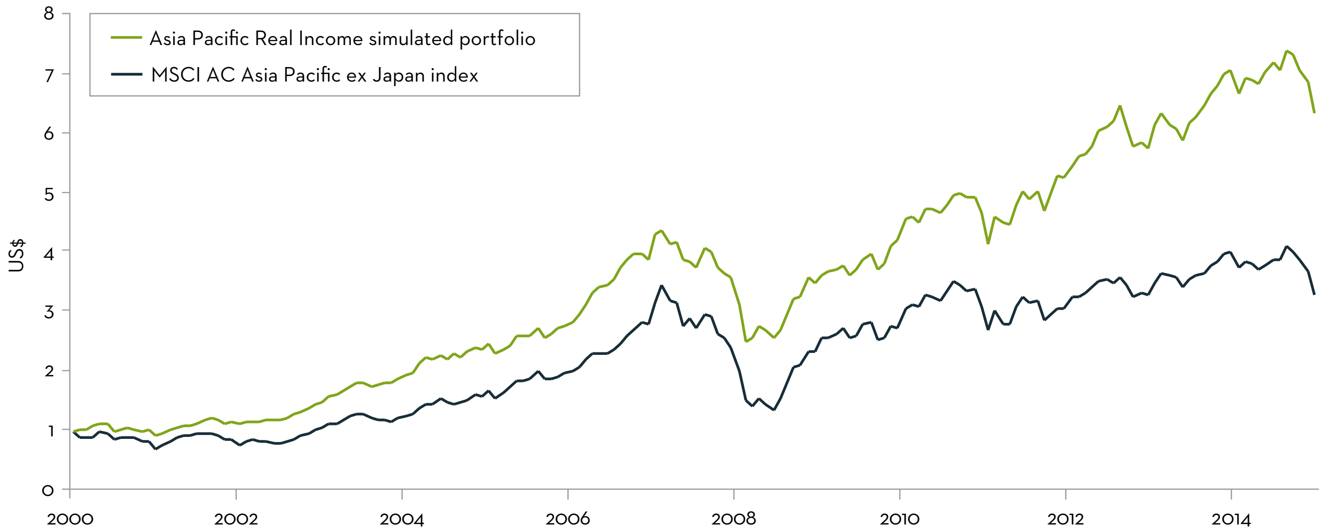
Total returns of the simulated portfolio and the market are shown in the chart below.

Chart 6: Asia Pacific Real Income simulated portfolio: total returns (value of US$1)



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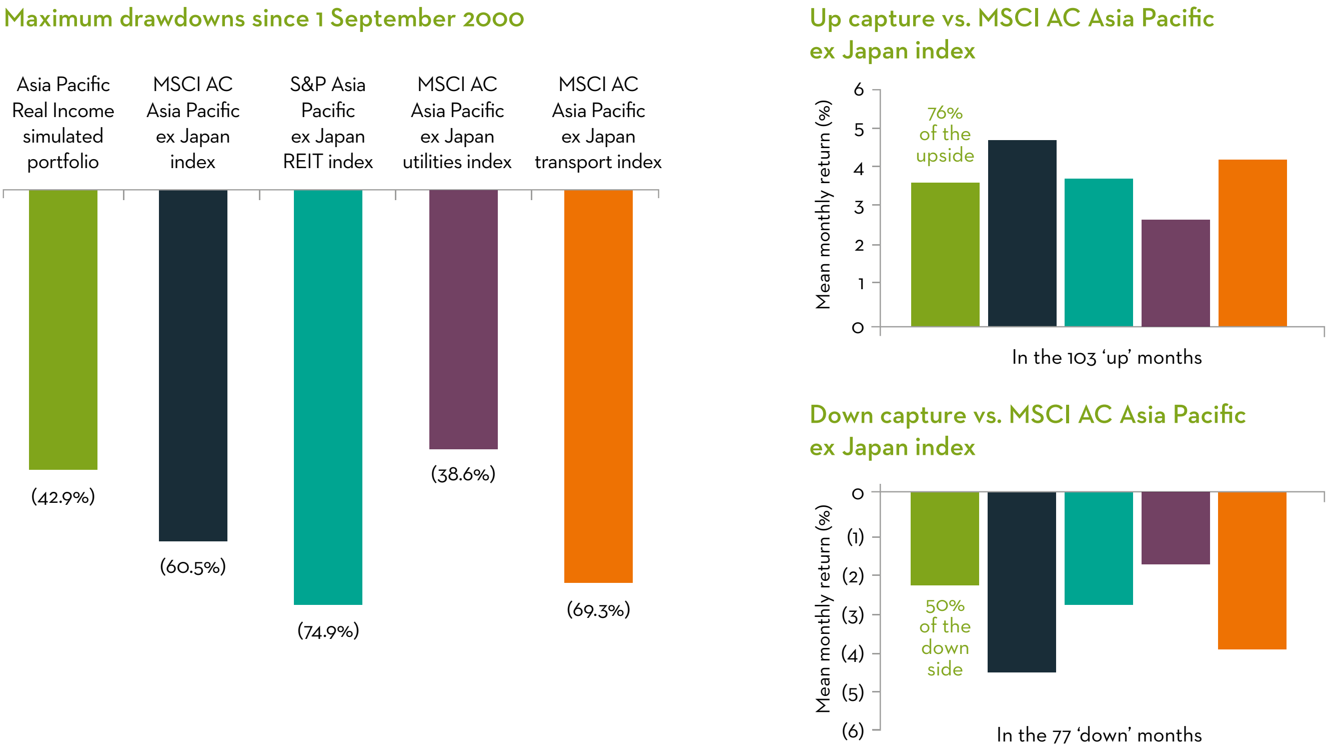
Total returns of the screen universe have proven to be very resilient in volatile market conditions. The following chart highlights the attractive up/down capture and low drawdowns of the simulated portfolio relative to the market and sub-sectors.

Chart 7: Asia Pacific Real Income simulated portfolio: drawdowns and up/down capture



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The following charts also illustrate the consistency over time of the lower risk/better return characteristics of the simulated portfolio.

Chart 8: Asia Pacific Real Income simulated portfolio: portfolio local beta

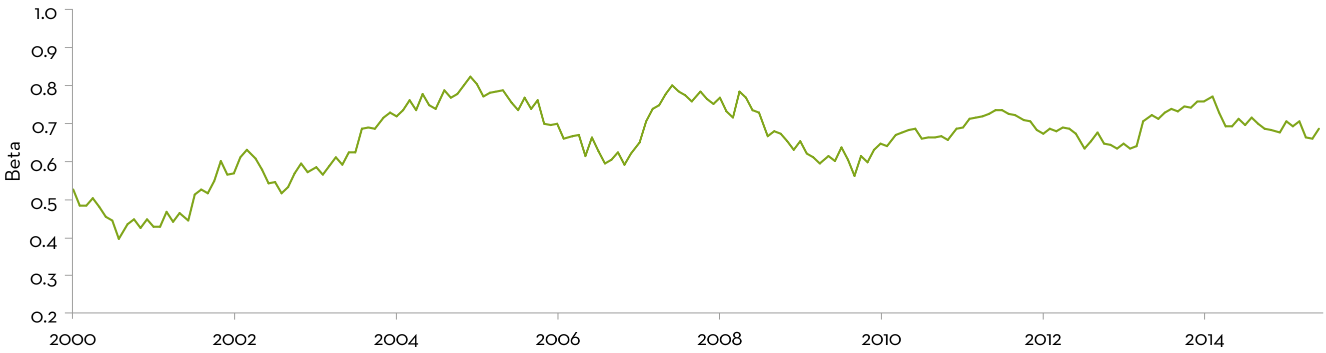

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Chart 9: Asia Pacific Real Income simulated portfolio: portfolio forward yield (next twelve months)

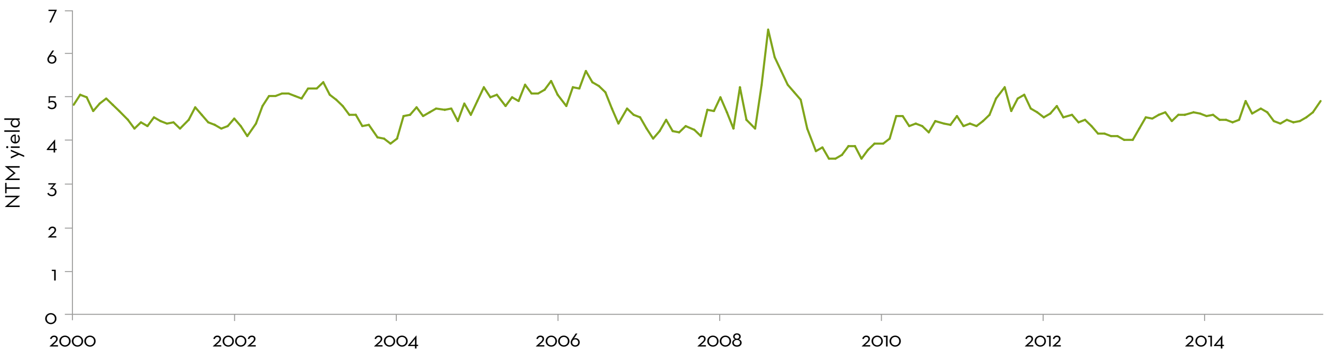

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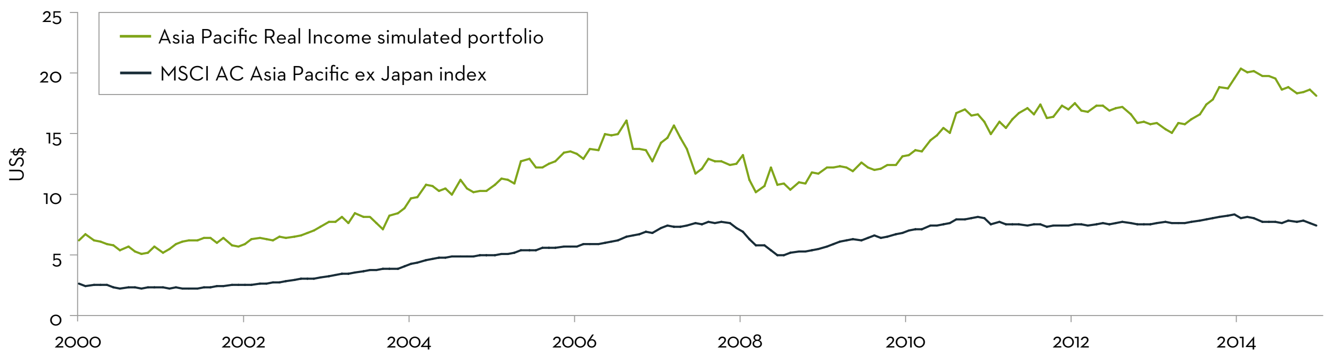
Chart 10: Asia Pacific Real Income simulated portfolio: next 12 month income from US$100 invested 15 years ago



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MODEL PORTFOLIO

Having proven the efficacy of the investment case and confirmed the scale of the investment universe over the prior 15-year period, Martin Currie Australia commenced a model portfolio version of the strategy on 31 May 2015 to test the thesis.

Through detailed analysis and active stock selection, the simulated portfolio from the back test was further refined by our analysts. Our analysts reviewed stocks for the model portfolio based on a deep understanding of each asset's valuation, quality, direction and sustainable dividend, from both a fundamental and quantitative perspective. Martin Currie Australia believes that the combination of these four different investment factors can lead to stronger income and capital returns over the long term than a focus on any one factor can deliver on its own.

The table below highlights the performance of the model portfolio, the market and relevant sub-sectors, on a monthly basis since 31 May 2015. The chart highlights the cumulative monthly performance.

Table 2: Asia Pacific Real Income model portfolio: total returns

Month ending	Asia Pacific Real Income model portfolio (%)	MSCI AC Asia Pacific ex Japan index (%)	Relative return vs. model portfolio (%)	S&P Asia Pacific ex Japan REIT index (%)	MSCI AC Asia Pacific ex Japan utilities index (%)	MSCI AC Asia Pacific ex Japan transport index (%)	Average of the three sectors (%)	Relative return vs. model portfolio (%)
Jun-15	(2.77)	(3.85)	1.09	(2.47)	(4.27)	(5.29)	(4.01)	1.25
Jul-15	(0.87)	(4.98)	4.12	(0.20)	(0.70)	(2.63)	(1.18)	0.31
Aug-15	(5.31)	(10.12)	4.81	(8.09)	(8.38)	(7.34)	(7.94)	2.62
Sep-15	(1.04)	(2.28)	1.24	(0.77)	0.60	0.50	0.11	(1.15)
Oct-15	7.53	7.54	(0.01)	7.12	5.66	5.43	6.07	1.47
Nov-15	(0.46)	(2.51)	2.04	(1.44)	(4.70)	(1.23)	(2.46)	1.99
Dec-15	1.73	0.35	1.38	2.59	1.73	(0.79)	1.18	0.55
Jan-16	(2.98)	(7.83)	4.86	(2.07)	(5.46)	(6.79)	(4.77)	1.79
Feb-16	4.52	(0.88)	5.40	3.90	1.45	2.42	2.59	1.93
Mar-16	8.21	11.57	(3.36)	8.44	10.48	9.31	9.41	(1.20)
Since inception (p.a.)	**7.92**	**(13.95)**	**21.87**	**6.10**	**(4.90)**	**(7.42)**	**(2.24)**	**10.17**

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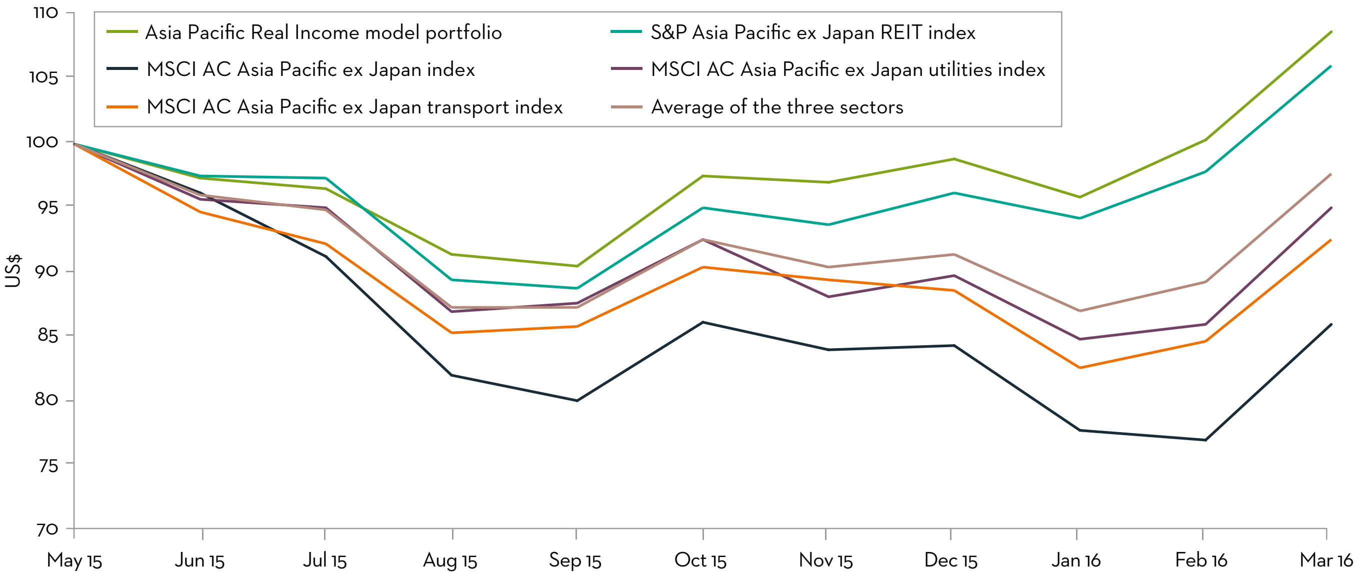
Source: Martin Currie Australia, Factset; for illustrative purposes only. Based on an un-audited Asia Pacific Real Income model portfolio to 31 March 2016 in US$. The performance data is presented net of investment advisory fees, broker commissions and all other expenses borne by investors. The annual fee rate used is 0.75% plus expenses. Model portfolio inception date: 31 May 2015. Theoretical results are shown without transaction costs that would reduce the return to investors. This strategy is not constrained by a benchmark but we show it versus the MSCI AC Asia Pacific ex Japan index for illustrative purposes only.

Chart 11: Asia Pacific Real Income model portfolio: total returns (value of US$100)



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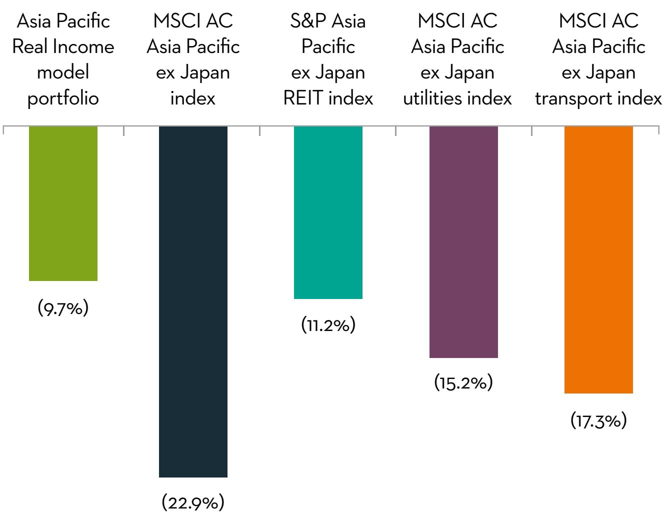
Since 31 May 2015, The Asia Pacific Real Income model portfolio has outperformed the MSCI AC Asia Pacific ex Japan index by 23%, and importantly, each of the relevant sector indices.

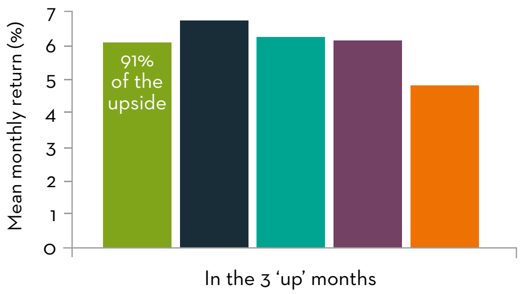
Over the period, it has also proven to be even more resilient in volatile market conditions than the simulated portfolio back test. The following chart highlights the attractive up/down capture and low drawdowns of the model portfolio relative to the market and sub-sectors.

Chart 12: Asia Pacific Real Income model portfolio: drawdowns and up/down capture

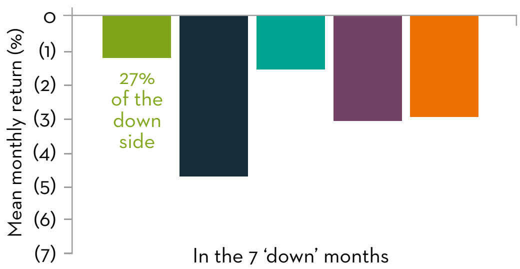
Maximum drawdowns since 31 May 2015



Up capture vs. MSCI AC Asia Pacific ex Japan index



Down capture vs. MSCI AC Asia Pacific ex Japan index



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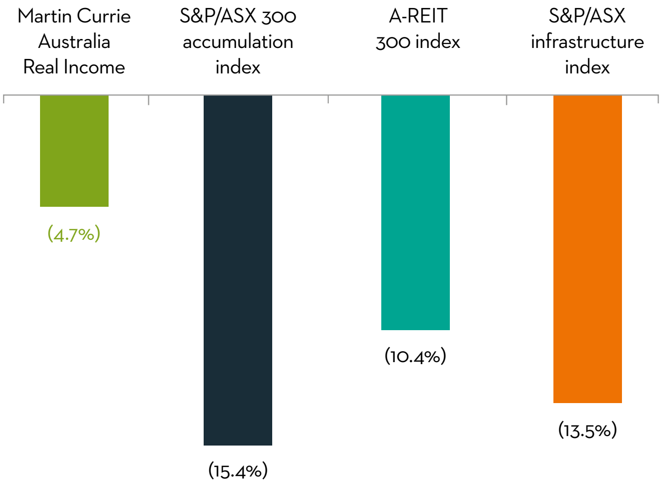
The strategy is managed by the same investment team as Asia Pacific Real Income.

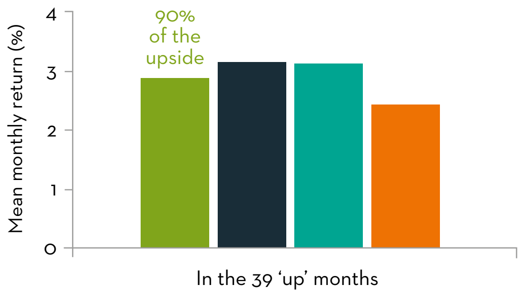
These outcomes repeat the experience of our long-standing Australia Real Income strategy, giving us the comfort to believe that the addition of active stock selection to the strategy will deliver outcomes consistent with client objectives.

Chart 13: Martin Currie Australia Real Income: drawdowns and up/down capture

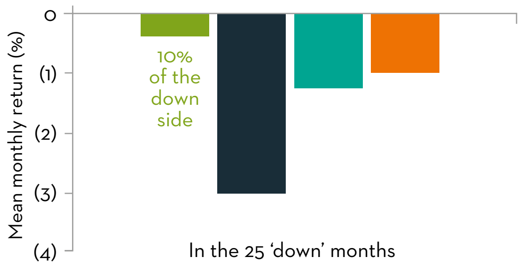
Maximum drawdowns since 1 December 2010



Up capture vs. S&P/ASX 300 accumulation index



Down capture vs. S&P/ASX 300 accumulation index



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The strategy is managed by the same investment team as Asia Pacific Real Income.

Please note that these performance figures are gross of management fees, and results for the model portfolio and simulated portfolio do not include transaction costs, brokerage or market impact. We expect the portfolio to have low turnover (approximately 30% p.a.), and therefore these costs will be negligible. Our analysis has indicated that these costs should be expected to be no more than what we have experienced in the Australia Real Income strategy.

CONCLUSION

Deutsche Bank was asked to carry out this research to test the strategy's investment belief. That is, that listed real assets in the Asia Pacific ex Japan region can meet the needs of investors requiring an attractive and growing income stream, with less volatility than the broader equity market. The findings of this analysis indicate:

- The Asia Pacific Real Income simulated portfolio was able to deliver not only better income, but also better growth, and a better total return with less volatility and lower drawdowns than the MSCI AC Asia Pacific ex Japan index over the back-test period.
- The simulated portfolio was also able to provide higher returns and lower volatility than sector specific indices.
- The lower risk/better return characteristics of the universe have been consistent over the time of the back test.
- The range of potential returns within the simulated portfolio could be further enhanced by stockpicking, as proven in the model portfolio and supported by the evidence of the Australia Real Income strategy since inception.

We fully recognise that back tests have flaws and we have aimed to neutralise these by appointing an independent agent to test the efficacy of our thesis. We have further tested the proposition through the introduction of our model portfolio. Finally, we are also able to evidence our capabilities based on our existing Australia Real Income strategy. It is the combination of these three components that gives us the conviction to launch the Asia Pacific Real Income strategy.

We believe that this transparent and evidence based analysis enables investors to weigh up the benefits of this investment approach, as we see this as a unique proposition that is desirable for income investors and those seeking an attractive risk-adjusted total return.

FIND OUT MORE

For further information on the Martin Currie Australian equities range please visit our website – **www.martincurrie.com**
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