

WealthStyles

Income Series, Part 1 of 3

Income investing: The secret to financial health

Key takeaways

- Income investments can generate cash flow that may help to ease any financial burdens – this is important for retirees
- Those still working can achieve potentially greater returns by reinvesting their income payments – a reminder to perform regular portfolio reviews

The sudden emergence of COVID-19 has left a major dent in the global economy. To comply with regulatory requirements, some international banks cut or even suspended their dividend payouts last year without warning¹. As a result, many investors who rely on dividends have been left in the lurch. How important is income to investors?

Bruno Lee, Regional Head of Retail Wealth Distribution, Wealth & Asset Management, Asia at Manulife Investment Management points out that global central banks have been implementing quantitative easing measures for years. This attempt to stimulate the economy by substantially increasing money supply has prolonged the low-rate environment, which, in turn, makes it harder for investors to generate income (It can take the form of cash dividend, interest, or coupon payments, while it doesn't come from buying or selling assets).

Income serves as an additional source of cash that allows investors to manage their daily expenses, for example. Something that is especially important for retirees, as they generally have to rely on their savings in the absence of a salary from paid employment. A steady investment income can also help to create an “alternative salary” by reversing the net cash outflow situation, which, in turn, alleviates the financial burden.

Younger people and those with established careers already have a regular salary, so they are probably more focused on capital gains. That's why an investment tool that offers income payouts is not necessarily their first choice.

In fact, the purchase of income-paying assets actually serves two functions: firstly, income can be reinvested to achieve greater potential returns (potential income plus capital gains). Secondly, it serves as a reminder to review one's portfolio regularly.

“Income-focused investments act as an *additional cash source* and help to *reinforce effective wealth-management*”

Bruno Lee

Regional Head of Retail Wealth Distribution,
Wealth & Asset Management, Asia
Manulife Investment Management



Regular portfolio health checks: a reminder

Investors may be unaware that besides acting as an additional cash source, income-focused investments help to reinforce effective wealth management.

Lee believes that it is common for investors to neglect wealth management due to their hectic work schedules or lifestyles. Investing in assets that offer regular dividends can, therefore, provide a cordial reminder when any payouts are made. In Lee's experience, whenever a distribution is received, the amount is directly deposited into his cash account and he gets a notification with details of that transaction. His account balance continues to rise with each payment. This has the effect of highlighting any idle assets and, consequently, the need to review his portfolio. Lee can then decide whether reinvestment is required – a cycle that allows him to remain a disciplined investor.

Lee reveals more about his strategy: "I hold different types of funds with regular payouts. When, after a few months, the accumulated income reaches a certain level, I would consider how to reinvest the newly gained capital. For instance, I can increase my current holdings or look for investment opportunities in other equity funds during a sell-off."

In terms of investment allocation, Lee says investors may consider taking a conservative approach for the principal coupled with flexible asset allocation according to the investor's risk tolerance, lifecycle stage, and wealth-management objectives. As for the additional income, more aggressive investors can select higher-risk tools in the pursuit of better potential returns, as it accounts for only a small proportion of the portfolio's total value.

Different income functions for different people



¹ Source: Prudential Regulation Authority (PRA) of Bank of England (BoE), 31 March, 2020; European Central Bank (ECB), 28 July, 2020; Bloomberg, 14 October, 2020. The PRA of BoE requested local banks to suspend cash dividend payouts and share buybacks until 2020 year-end, and the situation will be reviewed in Q4 2020. The ECB requested regional banks to suspend cash dividend payouts and share buybacks until 1 January, 2021. Statistics from Bloomberg show that 28% of Asia Pacific companies have announced dividend suspension or cuts.

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