PIAS
PROFESSIONAL INVESTMENT ADVISORY SERVICES

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CONTRIBUTORS

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The Future of Innovation

Technology companies just can't seem to catch a break at the moment. Following last year's massive rotation in investments out of growth-focused stocks, the recent collapse of Silicon Valley Bank has generated fresh concerns over the sector's ability to secure future funding given the lender's importance to the technology ecosystem.

The crucial question for investors today is: Where do we go from here? Many investors recognise that historically low interest rates have produced excesses, including high-flying technology stocks without the earnings to support them. That said, the fundamental tenet of buying innovative companies still makes sense for long-term investors.

Innovation and disruption

To be clear, innovation does not necessarily equate to invention. Invention is the creation of something new, while innovation is often an improvement on an existing product, service, idea, or method. In many instances, innovation simply entails integrating pre-existing products, services, or ideas. This may sound marginal, but sometimes small tweaks can result in profound changes.

The iPhone is one example. When Steve Jobs unveiled the product in 2007, he described it as the intersection of a cell phone, internet access and an MP3 player. None of these things were new. But integrating these three things created arguably one of the most innovative products of our generation.

Disruption is another term often associated with growth investing. This usually refers to an attempt to destroy an old, perhaps inefficient, way of doing things in favour of something better. Better could mean cheaper, faster, higher quality or more efficient.

Recalling the past

Innovation and disruption are often not apparent and may even be unintentional at first, but they can effectively address a need, desire, or problem.

Netflix, for example, was founded in 1997 to address the bricks-and-mortar video rental store problem of late fee charges. The company created a mailing system that allowed for unlimited DVD rentals with the promise of no late-return fees.

It was not until a decade later that Netflix evolved into a purely online video-streaming company, allowing customers to watch shows and movies over the internet for a fraction of the cost of a cable subscription. Netflix went on to disrupt movie theatres, cable companies, and is in the process of doing the same to Hollywood. This disruption is the result of a ripple that all started because consumers disliked paying late fees on video rentals.

A look at the future

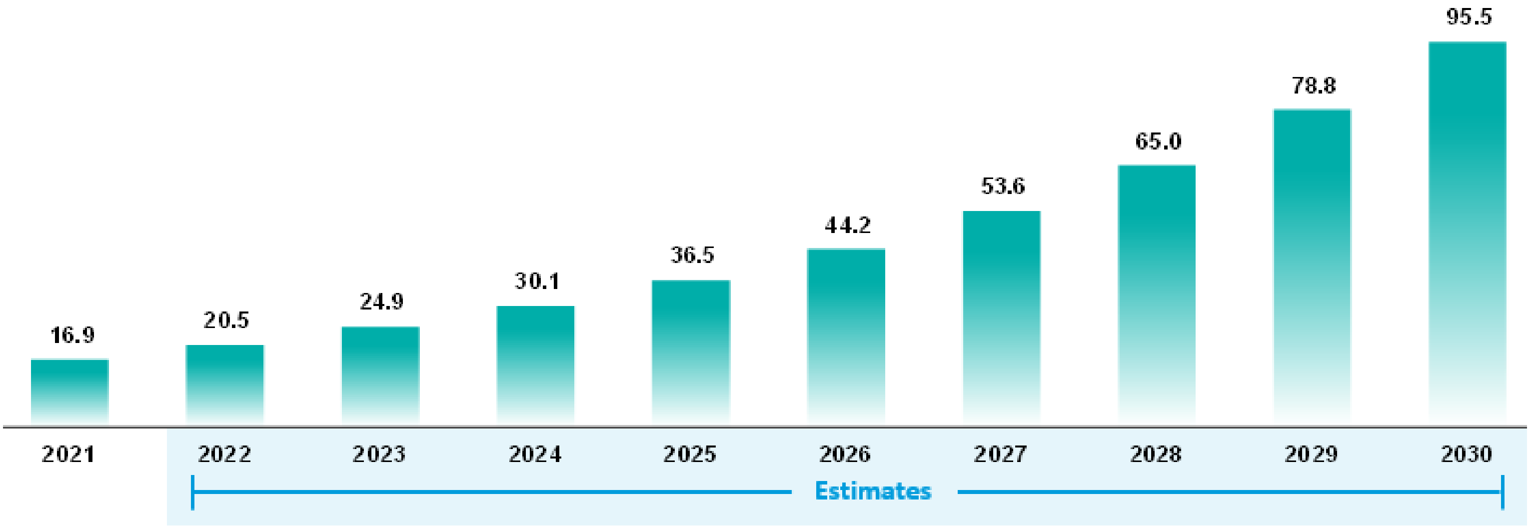
Looking ahead, just because growth stocks are out of favour does not mean that innovative companies can’t continue to prosper. We are seeing this in the healthcare sector, which is in the midst of a golden age of drug discovery.

Pharmaceutical companies have invested heavily in drug discovery in recent years and, as a result, deep pipelines of pioneering treatments are being developed to tackle some of the world’s biggest health issues. Eli Lilly and Novo Nordisk, for example, have developed obesity treatments with the potential to reduce body weight by as much as 25%.

Gene sequencing is another key innovation with major health and investment implications. In the future, genetic sequencing could be paired with gene-based interventions to deliver personalised, precision medicine. Imagine replacing defective or missing genes with normal, healthy ones. That future may not actually be that far off.

Gene therapies could reshape the future of healthcare

Global revenues from gene therapy and other regenerative medicine (USD billions)



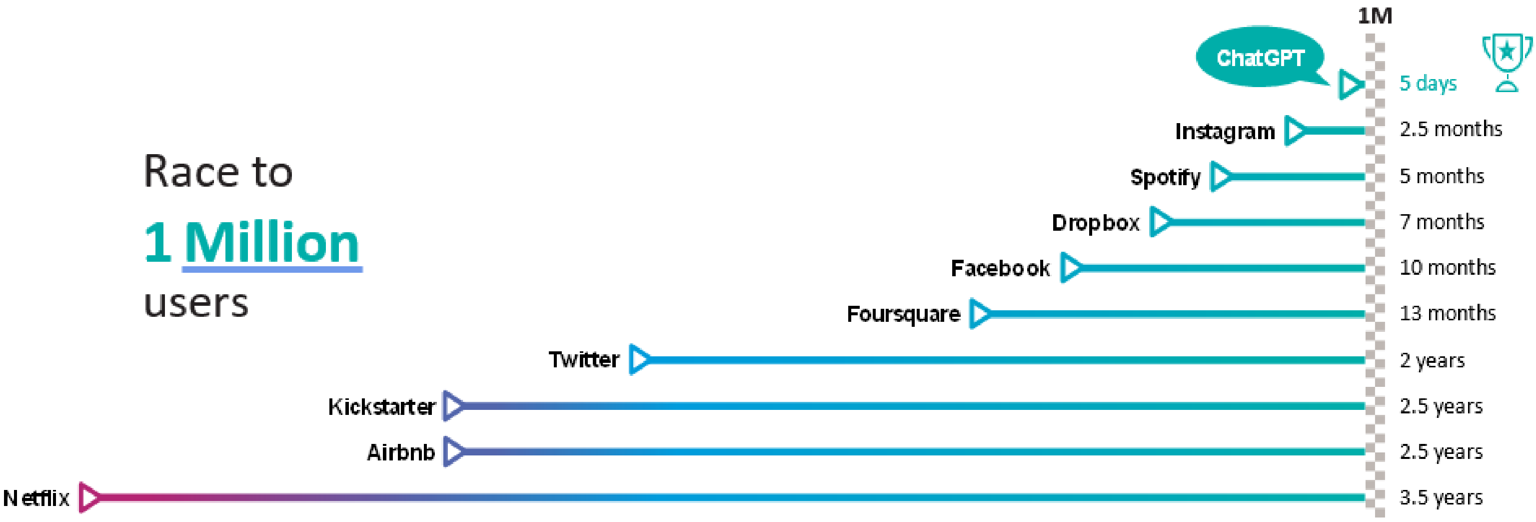
Forecasts shown for illustrative purposes only.
Data as at July 2022. Source: Statista

Outside of healthcare, there are also breakthroughs in the development of sophisticated programmes such as ChatGPT, which ignited investor interest in AI's (artificial intelligence) potential. Companies like Microsoft are already using AI technology to help differentiate their offerings and deliver enhanced productivity to customers. Microsoft has now issued a limited test release of its Bing search engine that harnesses ChatGPT. It also disclosed plans to include the technology in its widely used Office software suite, its Teams platform and its GitHub code-development service.

Microsoft isn't alone in its attempts to harness the power of AI. In fact, there is growing evidence that we may be entering an inflection point with AI, with more innovative uses of the technology occurring at a rapid speed.

The speed of adoption for new technologies is picking up

Time for selected online services to reach one million users



Data as at 31 December 2022. Source: Statista
Kickstarter refers to number of backers. Airbnb refers to number of nights booked. Foursquare and Instagram refer to number of downloads.

Another aspect of AI investing is that wider adoption of the technology will require massive computing power, providing tailwinds for cloud services and the semiconductor industry. So even though the technology remains at an early stage of development, many companies are already gearing up for what could potentially be the next driver of innovation and the long-term investment opportunities arising from this.

The future will undoubtedly look different in the way that 1997 now seems a lot different than today. But instead of always questioning what will change, considering what will not change could also be a useful thought exercise. People will still be busy and want choices, requiring everything to be faster, cheaper, better and more convenient in all aspects of their lives. Innovation and technology will continue to play a role in crafting a faster and more convenient future.

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Headquarters: Los Angeles

Founded: 1931

Assets under management: US $2.2 trillion (as at December 31, 2022)

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Why Asian High-Net-Worth Individuals Cannot Afford to Ignore Legacy Planning

Author | Article provided by Manulife Singapore

The majority of Asian High-Net-Worth Individuals (HNWIs) remain underprepared when it comes to legacy and succession planning. This can jeopardise both family harmony and the businesses they have worked so hard for.

As wealth continues to flow into the continent, the numbers of Asian HNWIs continue to increase. According to *Knight Frank's 2020 Wealth Report*, there are 103,335 HNWIs with a net worth of over US$30 million in Asia. While still trailing behind Europe and North America, its numbers are rapidly catching up, with a projected growth rate about double that of the West. It seems clear that Asian wealth will inevitably overtake its Western counterparts.

Much of this wealth comes from family-owned businesses. Ernst & Young estimates that at least 85% of companies in Asia-Pacific are owned by families. This naturally makes succession and legacy planning a top priority for the heads of these families—a finding confirmed in a 2019 research study by the *Asian Private Banker* surveying relationship managers on the behaviour of their Asian HNWI clients.

Yet, their actions are failing to match their words.

Most Asian HNWIs Remain Reluctant to Establish Definitive Successions Plans

Despite listing succession and legacy planning as their top priority, most Asian HNWIs have yet to implement any definitive plans. According to the same research study, a mere 40% of Asian HNWIs have or are currently planning a succession plan. Astoundingly, two-thirds of them said they have never even broached this matter with their families.

This is corroborated by other research, such as *UBS' 2019 Global Family Office Report*. It found that among family offices—which already implies a more structured and coordinated nature to managing familial wealth—only 49% of Asian family offices have succession plans in place, below the global average.

There are, of course, understandable reasons for this mismatch between actions and priorities. The topic of legacy planning encroaches on cultural taboos surrounding the discussion of death, leading to procrastination in even starting such a discussion. Despite this however, family heads must consider the very real risks of not having adequate succession plans in place. These include:

- Successors being unwilling or unable to take over the family business, jeopardising the future of the business.
- Potential disputes over the split of familial assets.
- Being unable to equitably split assets because of a large proportion being held in fixed assets or in the business.
- Inability to meet cash needs at death—e.g. from personal and family debts, discharging personal guarantees, as well as estate and inheritance taxes (in the case of foreign investments). This can create financial anxiety for family members and even necessitate the selling of fixed or business assets.

Not having enough cash to sustain themselves for a comfortable retirement after handing a business over. The UBS report notes that the average age of succession in Asia is 45, meaning the family head is likely to have at least several decades to enjoy their retirement.

Despite individual variations, the core of these challenges is largely universal to many Asian HNWIs. As such, the solutions to these challenges—such as universal life insurance plans—are similarly applicable across the board.

Life Insurance – A popular Solution for HNWI's Legacy Planning Challenges

For non-HNWIs, life insurance policies are often taken out to cover things like funeral costs and loss of income from the main income-earner. However, for HNWIs, who have little worries about sustaining the basic financial health of their families in the event of their passing, life insurance instead becomes a useful legacy planning tool.

The *Asian Private Banker* research study found that interest in life insurance among HNWIs continues to rise—ranking as the third most popular succession planning tool, behind cash equivalents and trusts. Interestingly, the greater the net worth of the individual, the more likely they would be to already have purchased a life insurance policy.

For instance, over 75% of HNWIs with over US$30 million in net worth had life insurance policies, compared to a mere 35% on those with a net worth between US$1 million to US$5 million. This indicates that the more successful the client, the more they realise the value of having such policies in place.

But if HNWIs don't need life insurance to compensate for funeral costs and loss of income, how does life insurance help them in constructing their legacy plans, particularly when each of them has different needs and circumstances?

Life Insurance – A popular Solution for HNWI's Legacy Planning Challenges

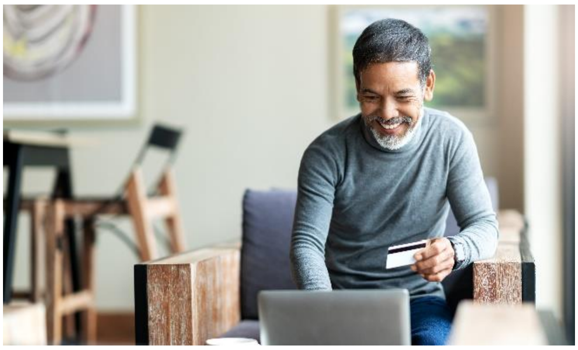
There are a variety of scenarios where universal life insurance can be invaluable in legacy planning. Two of the most common ones—which we will explore here—are to increase total estate size for a better retirement, and providing the necessary liquidity for equitable asset division.

Scenario 1 – Increasing total estate size for an improved retirement lifestyle

Consider a hypothetical HNWI, Mr. Lee, with a US$5 million net worth. US$2 million of this is tied up in his primary residence, while the other US$3 million is in cash and other liquid investments. He has two heirs that he wants to leave his estate to, but after a lifetime of hard work, he also wants to enjoy his retirement. He plans to retire within 10 years and savour several decades living a retired lifestyle.

However, he also wants to leave his heirs at least US$1 million each, plus his home, when he passes. To do that, he will have to live a more conservative retirement, as he will need to ensure at least US$2 million in liquid assets by the time he passes. He now faces a dilemma—either live more humbly or leave less for his heirs.

A universal life insurance policy can help resolve said dilemma. Say Mr. Lee pays a single premium of US$1 million for a policy with a death cover of US$3 million. That leaves him with US$2 million in liquid assets which he can spend in his retirement years. Upon his death, each of his heirs will receive US$1.5 million each—more than he intended—and he also gets more money with which to relish his retirement.



Scenario 2 – Generating estate liquidity to avoid forced selling of fixed or business assets

Now, let's look at another Mr. Lee, now a business owner with US$18 million in assets. He owns real estate worth US$6 million, his wholly owned business is worth US$6 million, and he has US$6 million in other liquid assets. He also has three heirs, but only one of them is willing and capable of taking over the family business.

His dilemma is now different—how does he ensure an equitable division of assets between his heirs without needing to sell off business assets or real estate? He also wants to leave each heir with some amount of liquid assets while keeping everything balanced. Finally, he would also like to set aside some cash for himself.

He chooses to pay US$2 million in premiums to buy a universal life policy with a death cover of US$6 million. Up till his passing, he spends US$1 million in cash.

Upon his passing, his estate value will have increased to US$21 million - i.e. US$6 million in real estate, US$6 million in his business, and US$9 million in cash. Now, he can divide his assets as follows:

- US$6 million in his business + US$1 million in cash for Heir 1
- US$6 million in real estate + US$1 million in cash for Heir 2
- US$7 million in cash and liquid assets for Heir 3

Legacy Planning is about Having Options – Life Insurance Can Give You Those Options

In the finance world, there is something known as a 'liquidity premium', which is the extra return investors demand for non-liquid investments. The liquidity premium only exists because liquidity is valued, as it gives investors options—such as the option to move in and out between investment opportunities and adjust their portfolios quickly.

Similarly, when planning your legacy, you, as an HNWI, want options. The option to divide your assets as you see fit. The option to enjoy a lavish retirement, while still leaving more to your heirs. There's a reason those with the highest net worth also have the highest likelihood of using universal life insurance policies—because they know the value of the options to them when it comes to their legacy plans.

If you're interested in learning more about how Manulife's Signature Solutions can help you in your legacy planning, please consult and speak to your trusted financial advisor today.

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PIAS Investment Outlook (Q2 2023)

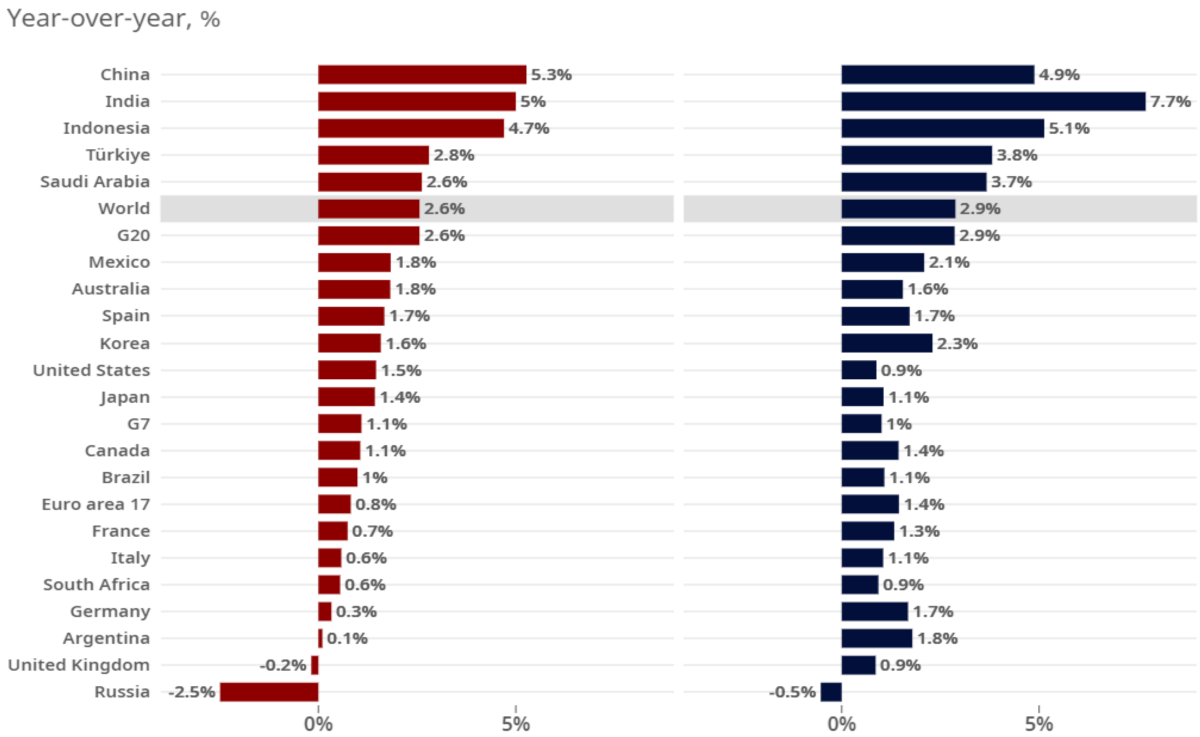
Author | Tan Yong Feng, Investment Strategy, Partnership Management | PIAS

Source | Figures extracted from Refinitiv Datastream, Fathom Consulting and Refinitiv Lipper Data, Reuter Graphics

The financial market was spooked in March, following the collapse of Silicon Valley Bank and Signature Bank which raised the fear of a domino effect of failing banks. Fortunately, the banking crisis was relatively contained after swift policy intervention from the regulators managed to shore up confidence in the banking system. Despite some of the market turbulence, major central banks did not dial back on their interest rate hikes. In March, the European Central Bank (ECB) raised its policy rate by 50 basis points whereas the Federal Reserve and the Bank of England lifted their benchmark rates by 25 basis points. All echoed the necessity to rein in stubborn inflation. “Higher for longer” seems to be the norm with regard to the tightening cycle of the central banks. **Although overall inflation has predominately peaked for most economies, core inflation remained sticky. OECD has forecasted that global real GDP growth is estimated to grow by 2.6% in 2023 (Chart A).**

In the US, inflation figures have moderated to 6.4% and 6% in January and February respectively. This is considerably lower than its peak of 9.1% in June 2022. However, this is still not remotely close to the Federal Reserve’s target rate of 2%. As the US inflation remains sticky and elevated, we believe that a Fed policy pivot is not expected in the near term. However, despite challenges stemming from the banking crisis, tightening of monetary policy and high inflation, we retain our neutral view of the US. **We believe that an economic downturn would be cushioned by robust employment, consumption, and a build-up of household income growth. The US economy has thus far been more resilient than initial projections and momentum could spill over to the following quarter. Although there is the likelihood of a US recession, we believe that should one occur, it will be a short and shallow recession.**

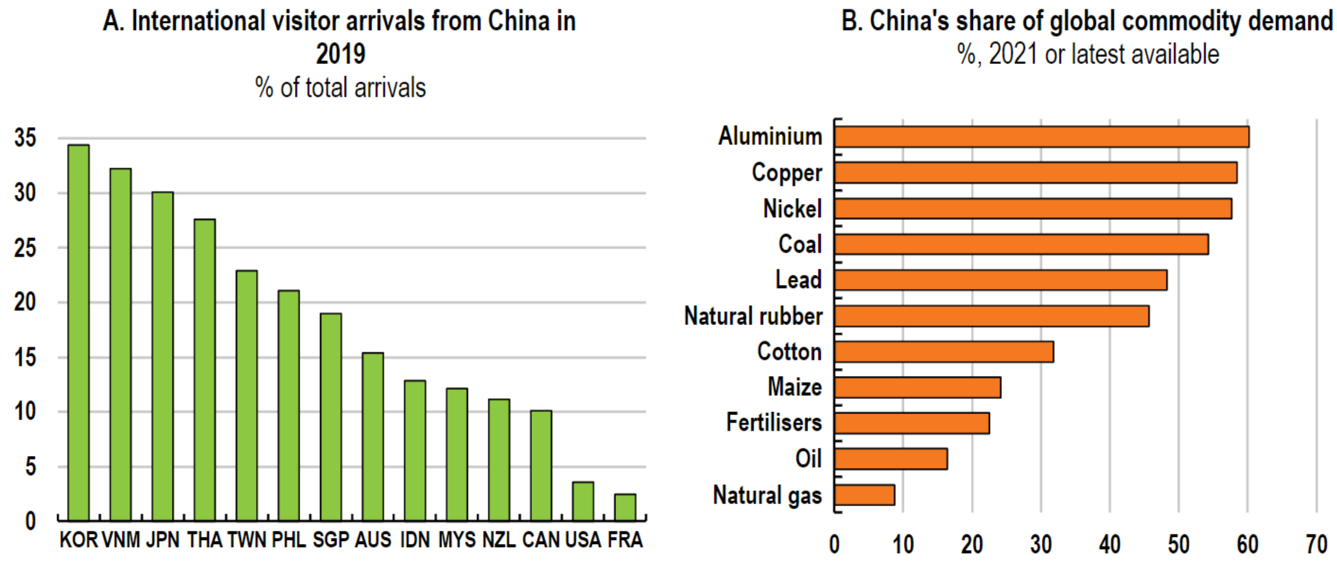
Chart A: Real GDP growth projections for 2023 and 2024



Source: OECD, March 2023

In Europe, the risk of a gas crisis had eased considerably in recent months, with Europe's gas storage and supply holding up. Although this has helped ease some of Europe's inflationary pressure, the Eurozone inflationary pressure persisted due to rising food prices, lingering effects from past supply bottlenecks and persistent higher wage growth. With the enduring inflation, the ECB raised its benchmark interest rate by 50 basis points on 16 March which cumulates to a 15-year high of 3.0%. The ECB continued its hawkish stance as President Christine Lagarde said "Inflation is projected to remain too high for too long" and the ECB "stands ready to respond as necessary to preserve price stability and financial stability" in the eurozone. **Our view remains slightly negative as ECB maintains its tightening cycle to combat inflation, thereby increasing the possibility of a recession. We believe that the headwinds from elevated interest rates and inflation would more than offset the positivity from fading energy shock and boosts to European exports originating from China's reopening.**

Chart B: Reopening of China will affect global demand



Source: OECD, March 2023

The relaxation of China's Covid-19 policy at the turn of the year had market participants hopeful that it will ease the global economic slowdown. **We believe that the reopening of the world's second-largest economy is expected to have a positive impact on global activities as it eases the supply chain squeeze and boosts international tourism (Chart B)**. At the National People's Congress (NPC) in March, China had announced a 2023 GDP target of 5% and proposed a slight increase in its fiscal support by expanding the budget deficit target from 2.8% in 2022 to 3% in 2023. Pro-business policies in support of large private corporates and extra stimulus aimed to revive the real estate sector were also put forth by the Chinese Communist Party. **We believe that China's pent-up domestic consumption and muted inflation will guide China to a sharper recovery than initially expected. With those backdrops, we have upgraded our view in China to slightly positive. Although geopolitical tensions remain and its property sector remains weak despite a recent turnaround, the strong fundamentals of China's economy will support China in rebuilding its covid-reopening recovery**.

While the short-term global economic outlook has improved, mainly driven by the reopening of China and the peaking of inflation across most economies, we are mindful that downside risks still predominate from the continued tightening of monetary policy, trade tensions and geopolitical conflicts. We are careful that the global recovery remains fragile. As such, we recommend investors to stay invested in a well-diversified portfolio while seeking opportunities during the downturns.

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Integrity
Doing the right things.

Accountability
Taking ownership.

Synergy
Capitalising on our individual abilities to achieve shared organizational goals and visions.

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Head Office
6 Shenton Way, OUE Downtown 2,
#09-08, Singapore 068809

T: +65 6372 5700
F: +65 6372 5950
E: pias.enquiry@singlife.com
W: www.proinvest.com.sg

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