

Income Strategies for a Low-Rate Environment

We believe an equity income strategy remains an attractive long-term option for investors looking for a stable income stream by way of dividend payments.

The Case for Equity Income Investing

Equity income investing is popular because of the regular payments of dividends, the possible tax benefit offered by franking credits, and low interest rates offered by traditional income sources such as cash deposits.

But recent market volatility has some investors asking, is an equity income strategy still a worthwhile option?

We believe an equity income strategy remains an attractive long-term option for investors looking for a stable income stream by way of dividend payments. In the sections that follow, we will explain the potential benefits and risks of this strategy as well as offer a fresh take on income investing offshore.

Why an Equity Income Strategy?

In the search for income, investors have a number of strategies or asset classes to choose from. Equity income strategies deliver dividends, fixed income strategies deliver interest coupon payments, and cash strategies deliver daily or monthly interest payments.

An equity income strategy has the potential to:

1. Enhance Income

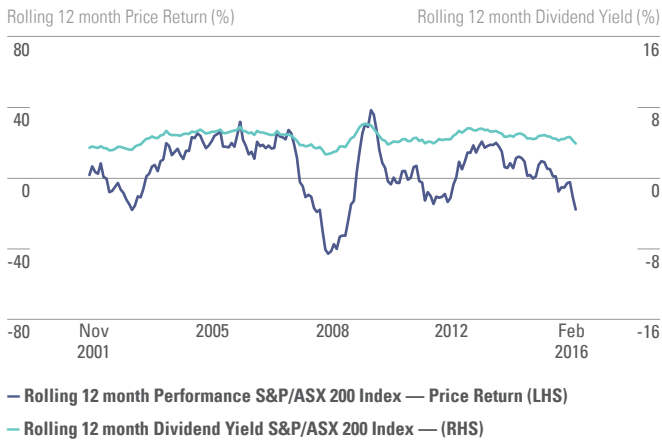
With low interest rates, cash and term deposits may not be able to provide you with the level of income you need to match your liabilities. The average one-year term deposit rate has dropped significantly over the past five years, from 6.1% p.a. at end February 2011 to 2.40% p.a. at end February 2016.¹

An equity income strategy offers an opportunity to boost your income return. Figure 1 shows that the current yield of the S&P/ASX 200 index exceeds the prevailing average one-year term deposit rate. The chart also shows that you would have earned more from yield than from the share price return of the S&P/ASX 200 over the last 14 years.

What to be Aware of: Companies are able to cut or stop paying dividends at any time and this is particularly true during times of crisis. For example, during the Global Financial Crisis a number of companies either suspended or cut dividends as companies sought to preserve capital. Investors need to consistently monitor any changes in a company's dividend policy. In addition, monetary policy can change leading to an increase in interest rates that, in turn, could result in bonds and deposits providing better income returns than dividends.

Income Strategies for a Low-Rate Environment

Figure 1: Stability of Dividend Income Versus Growth in Global Shares (Including Reinvestment)



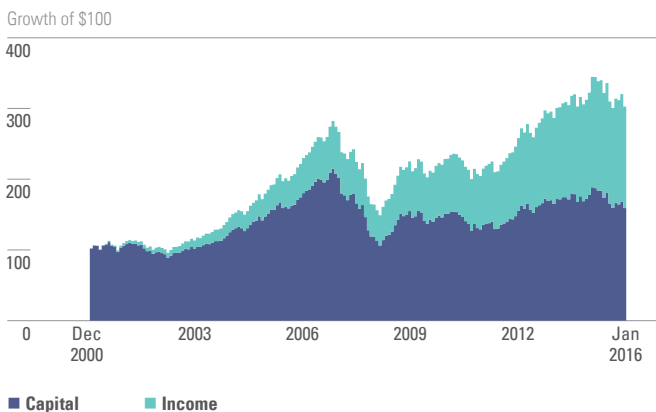
Source: SSGA and S&P, as of 29 February 2016.

Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income. Past performance is not indicative of future performance.

2. Provide Stable Returns

Over the last 10 years, income returns have provided a significantly larger proportion of an investor's total portfolio growth as compared to capital returns. The chart in Figure 2 shows stable income returns for both the broad S&P/ASX 200 Index and the MSCI Australia Select High Dividend Yield Index (which represents high yield dividend paying companies) over the last 15 years. And because income returns have been consistently higher than returns from capital growth (or share price appreciation) during this period, they have supported total equity returns in times of market downturns.

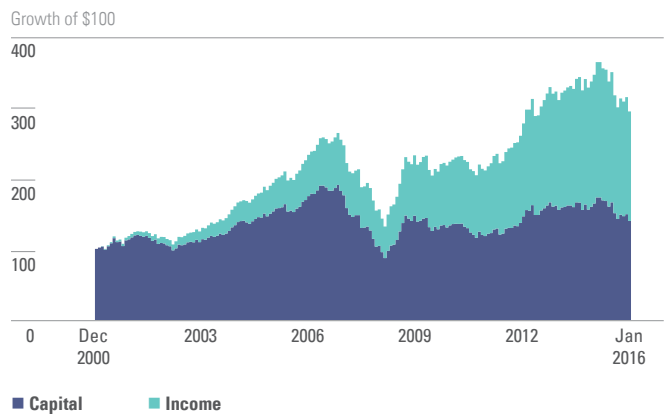
Figure 2A: S&P/ASX 200 Index



Source: S&P, as of 31 January 2016.

Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income. Past performance is not indicative of future performance.

Figure 2B: MSCI Australia Select High Dividend Yield Index



Source: MSCI, as of 31 January 2016.

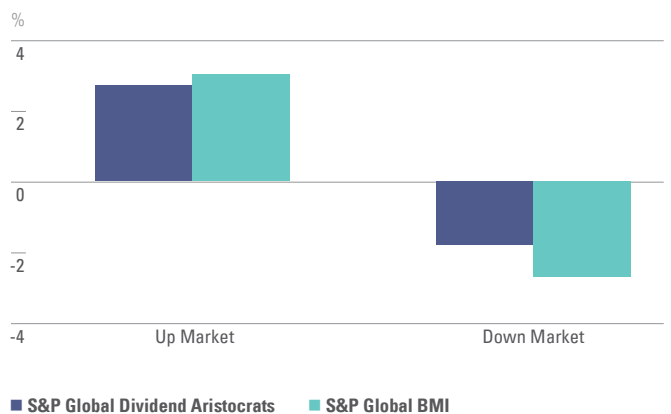
Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income. Past performance is not indicative of future performance.

What to be Aware of: Past performance is not a reliable indicator of future performance. While equity income strategies may be less volatile than other equity strategies, they still introduce more volatility compared to a cash investment. Investing in equity income strategies need to be taken with a long term view.

3. Participate in Rising Markets and Cushion Against Down Markets

Globally, high quality equity income strategies have offered the opportunity to participate in market upswings, while providing potential downside protection in turbulent times. Figure 3 shows that the S&P Global Dividend Aristocrats

Figure 3: Average Monthly Return in Up and Down Market

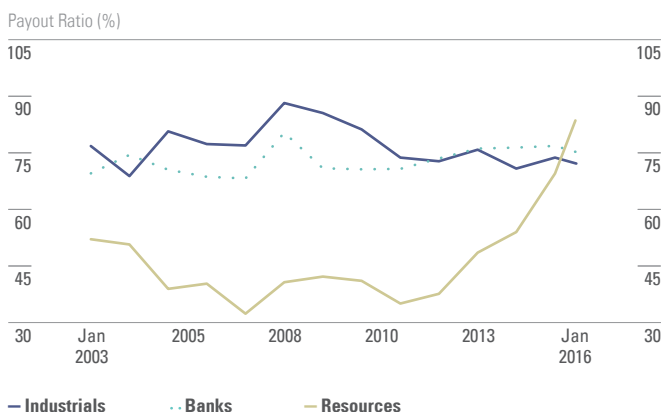


Source: S&P, as of 29 February 2016.

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Income Strategies for a Low-Rate Environment

Figure 4: S&P/ASX 200 Index Payout Ratio



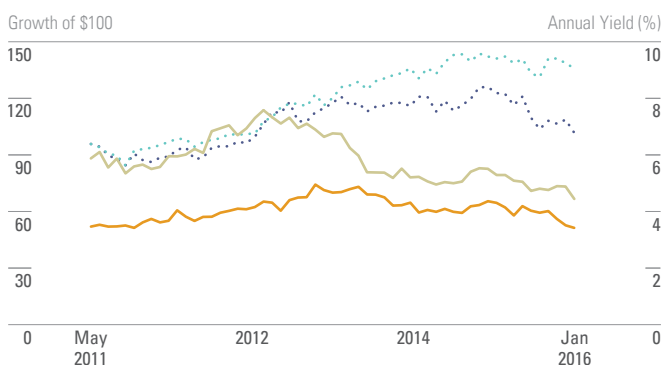
Source: Bloomberg, S&P, Deutsche Bank, IBES, Datastream, as of 14 January 2016.

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Index held up relatively better than the broad market S&P Global Broad Market Index in down markets, while performing nearly at par in upmarkets over a 20 year period from 31 January 1996 to 29 February 2016.

A reason for this is the element of quality that is introduced to an equity strategy, particularly if the strategy moves beyond pure yield and focuses on companies that have a consistent record of growing dividends as well. (Quality characteristics may be defined by return on equity, debt to equity, and variability of earnings.). Companies that have shown an ability

Figure 5: High Yield Indices



· · MSCI Australia Select High Yield Index (local currency, price return)
 · · S&P High Yield Dividend Aristocrat Index (local currency, price return)
 — MSCI Australia Select High Yield Index (local currency, rolling 12 month yield)
 — S&P High Yield Dividend Aristocrat Index (local currency, rolling 12 month yield)

Source: S&P, MSCI, Factset, as of 31 January 2016.

Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income. Past performance is not indicative of future performance.

to consistently grow their dividends over time tend to have stronger balance sheets and businesses.

What to be Aware of: An equity income strategy will not always outperform the return on a broad market index like the S&P/ASX 200 or the S&P 500. It is not uncommon for high quality companies to go through periods of underperformance relative to other companies, such as high growth companies.

Considering Global Equities

It can be difficult to create a diversified equity income portfolio in Australia because of the market's concentration toward financials and resources companies. Figure 4 shows that the resources sector has been the dominant driver of increasing dividend payout ratios in recent years, but that has recently been clouded in uncertainty because of the industry's outlook.

One way of increasing diversification is by investing in global equities. Global equities as a source of income may have been overlooked in recent times partly because dividend yields of the global equity broad market index (MSCI World ex-Australia Index) has trailed dividend yields of the S&P/ASX 200 over the last 10 years.² But there are now attractive opportunities in global equities.

Figure 5 shows that the gap between Australian high yield equities and global high yield equities is narrowing, making global equities an attractive option for income-focused investors.

Previously available only to institutional investors, global equity income strategies are now easily accessible using cost-efficient ETF products as building blocks of an income portfolio.

Although international high yield investments do not carry franking credits, they may offer investors other benefits that have the potential to enhance overall portfolio performance, including access to attractive equity valuations in potentially undervalued markets and benefit from structural trends across the global economy, including growth in emerging markets.

However, investors should consider that foreign exchange fluctuations and political risk may impact the investment outcome.

Quick Summary

	Australian Equities	Global Equities
Franking Credits	Yes	No
Diversification	Limited diversification because of dominance of the financial and resources sectors	Bigger universe of companies, across sectors and regions
Risks	Concentration risk	Currency, political risks

Income Strategies for a Low-Rate Environment

Conclusion

In today's low rate environment, equities can provide attractive income returns compared to cash or bonds and offer a potential stable income stream for investors. However, investors need to take into account the Australian market's concentration when building their equity income portfolio and consider global equities to improve diversification.

Investors must balance the benefits of the strategy with potential risks, including the risk that companies may cease to issue dividends or reduce their payouts in difficult markets, as well as currency and political risks related to global investing.

SPDR ETFs for Income Investing

Our suite of SPDR ETFs allows investors to build a diversified income or yield seeking portfolio.

Fund	ASX Code	Benchmark	Description	Management Costs (%)	Dividend Yield* (%)
SPDR S&P Global Dividend Fund	WDIV	S&P Global Dividend Aristocrats Index	Tracks an index representing high yielding companies from the S&P Global Broad Market. Index with a history of stable or increasing dividends.	0.50	5.30
SPDR Dow Jones Global Real Estate Fund	DJRE	Dow Jones Global Select Real Estate Securities Index	Tracks an index representing global REITs and real estate operating companies.	0.50	3.71
SPDR MSCI Australia Select High Dividend Yield Fund	SYI	MSCI Australia Select High Dividend Yield Index	Tracks an index of listed Australian securities that aims to achieve a higher than average dividend yield.	0.35	6.34
SPDR S&P/ASX 50 Fund	SFY	S&P/ASX 50 Index	Tracks an index of the 50 largest securities by market capitalisation in Australia.	0.286	5.55
SPDR S&P/ASX 200 Financials Ex A-REIT Fund	OZF	S&P/ASX 200 Financials Ex-A-REIT Index	Tracks an index of listed Australian securities involved in the financial sector (except those that are classified as Australian Real Estate Investment Trusts).	0.40	6.50
SPDR S&P/ASX 200 Listed Property Fund	SLF	S&P/ASX 200 A-REIT Index	Tracks an index of the leading listed property vehicles in Australia and represents diversified exposure to the Australian listed property market.	0.40	4.79

* Dividend yield is at 29 February 2016. Past performance is not indicative of future performance.

¹ RBA Statistical Tables, Retail Deposit and Investment Rates, March 2016.

² Source: SSGA, S&P, MSCI and Factset, 31 January 2016.

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State Street Global Advisors Australia Services Limited Level 17, 420 George Street, Sydney, NSW 2000. 1300 665 385.

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