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Portfolio Manager Insights

Manulife U.S. Regional Bank Trust

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Market Environment

The early part of the quarter was characterized by generally better U.S. economic data, higher oil prices and a weaker U.S. dollar. Federal Reserve officials made comments suggesting there could be additional interest rate increases in 2016. However, a weak U.S. jobs report in early June led to questions about the timing of future interest rate hikes. Then, in late June, the U.K. vote to leave the European Union ("Brexit") caused tremendous uncertainty in the global markets and further pushed out the expected timing of interest rate increases in the U.S.

Portfolio Review

Over the period, stock selection within the Financial sector contributed to the Fund's performance. With oil prices rebounding, the energy-exposed banks tended to outperform. Hancock Holding Company, Cullen/Frost Bankers, Inc. and Northrim BanCorp Inc. all posted double-digit returns for the quarter. Bryn Mawr Bank Corporation also contributed to performance when it reported better-than-expected earnings with strong loan growth, an expanding net interest margin and lower expenses. Digital Realty Trust, Inc. ("Digital Realty"), a data center real estate investment trust, outperformed on better fundamentals, including solid demand for leases and higher lease rates.

The Fund's underweight allocation in fixed income securities detracted from performance. Our alternative asset manager holdings also negatively impacted performance. Shares of Blackstone Group, L.P., Intermediate Capital Group plc and KKR & Co. L.P. declined on concerns that market volatility and Brexit could negatively affect their business activity.

We established a position in The First of Long Island Corporation through a capital offering in May, and increased the Fund's position in Equity Bancshares Inc. in light of its compelling valuation. We eliminated our position in Digital Realty as the stock hit our price target, and we reduced our position in Norwegian insurer Gjensidige Forsikring ASA on concerns about European stocks following the Brexit vote.

Outlook

In our opinion, we continue to find attractive investment opportunities in the U.S. bank sector. The U.S. economy continues to expand at a moderate pace, leading to solid loan growth for the banks. Although the expectations for future interest rate increases have been delayed, the banks are accustomed to operating in an environment of low interest rates. We believe they will look to find other ways to reduce expenses or to increase revenues to make up for an extended period of low interest rates. Also, lower longer-term interest rates may lead to a stronger mortgage market and higher revenue for the banks from increased mortgage activity. Credit costs remain low and the energy sector, an area of concern earlier in the year, is looking better as oil prices have moved higher, which may lead to fewer credit issues than previously expected.

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For more information, please speak with your advisor or visit manulifemutualfunds.ca

Manulife Investments