SINGAPORE DOLLAR BONDS- AN EFFECTIVE DIVERSIFIER

Against the current equity market volatility, Singapore dollar (SGD) bonds can play a key role in stabilising investors' portfolios, while also providing an attractive level of income. Good active managers can enhance yields and reduce risks. This is particularly pertinent in today's low rate environment, where investors may be tempted to reach for yield at the risk of compromising quality.

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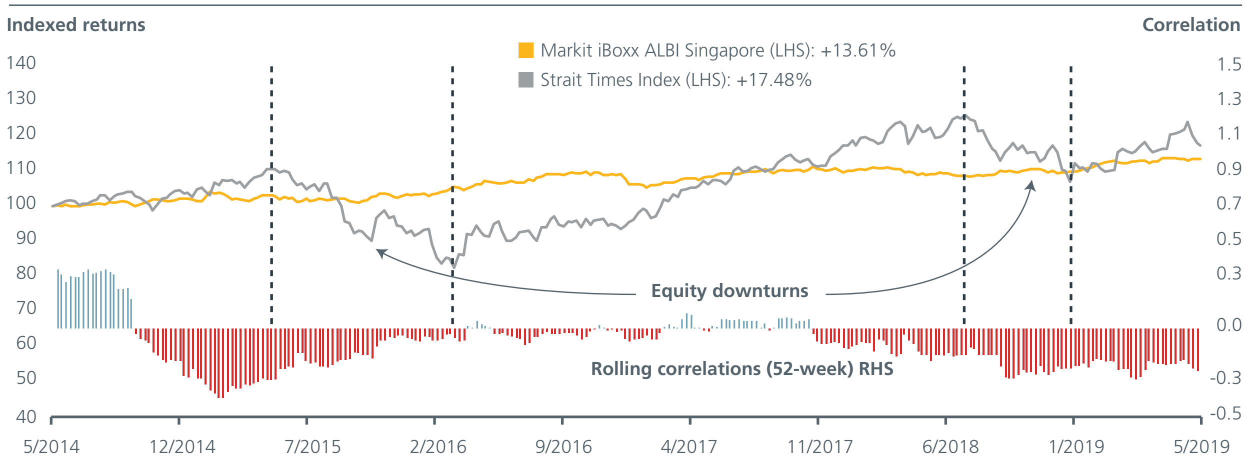
The SGD bond market, as measured by the Markit iBoxx ALBI Singapore index, has delivered a total return of 13.6% in the last five years.

The market has also exhibited remarkable stability during periods of equity market volatility. Rather than just holding ground, Singapore's local currency bonds generated positive returns even when the Straits Times Index sold off sharply in the first half of 2015 and the last quarter of 2018. See Fig. 1.

Fig. 1: Singapore dollar bonds delivered more stable returns[1]



The negative correlation between the SGD bond and the Singapore equity markets (see the lower panel of Fig. 1) implies that SGD bonds can play an important role in stabilising investors' portfolios over the medium to long term.

AN EFFECTIVE DIVERSIFIER FOR EQUITY RISK

Simply by adding some amount of SGD bonds into an all-equity portfolio allows investors to enjoy significantly lower volatility without giving up too much return.

Figure 2 shows that a portfolio consisting of 30% SGD debt and 70% Singapore equities (Portfolio B) would have achieved a 5-year annualised return of 3.11%. While the return is marginally lower than the 3.19% return from an all Singapore equity portfolio (Portfolio A), the volatility (measured by standard deviation) would have been significantly lower at 8.46%.

This translates into a higher risk adjusted return. The Sharpe ratio (a measure of return rate per unit of risk) for Portfolio B is 0.25; this is much higher than that of Portfolio A, which is only 0.18[3].

ENHANCE YOUR INCOME POTENTIAL

Compared to the yield offered by savings and fixed deposits, SGD bonds' average yield-to-maturity of 2.54% appears more attractive. See Fig. 3. That said, SGD bonds tend to have a longer duration and experience daily mark to market volatility.

It is, however, possible for investors to enhance their yield further through active professional management.

Fig. 2: SGD debt is an effective diversifier hedging equity risks[2]

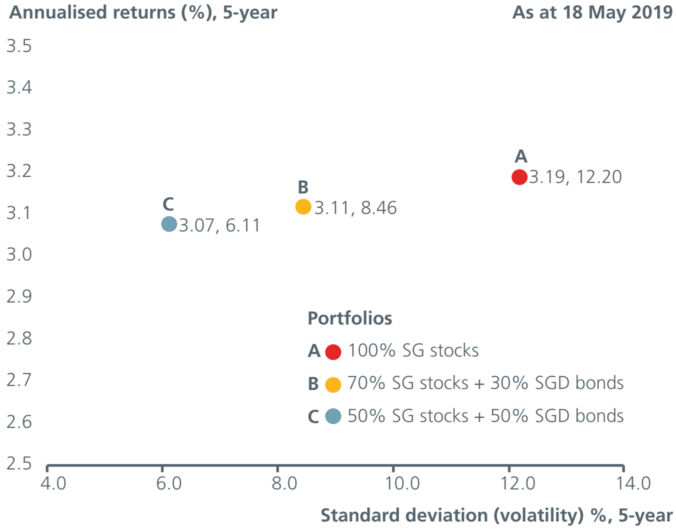


Fig. 3: Yield comparison of various SGD income option[4]

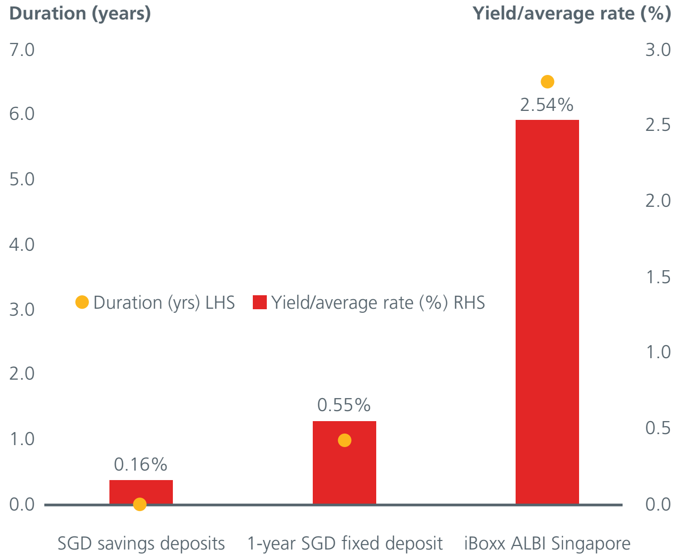
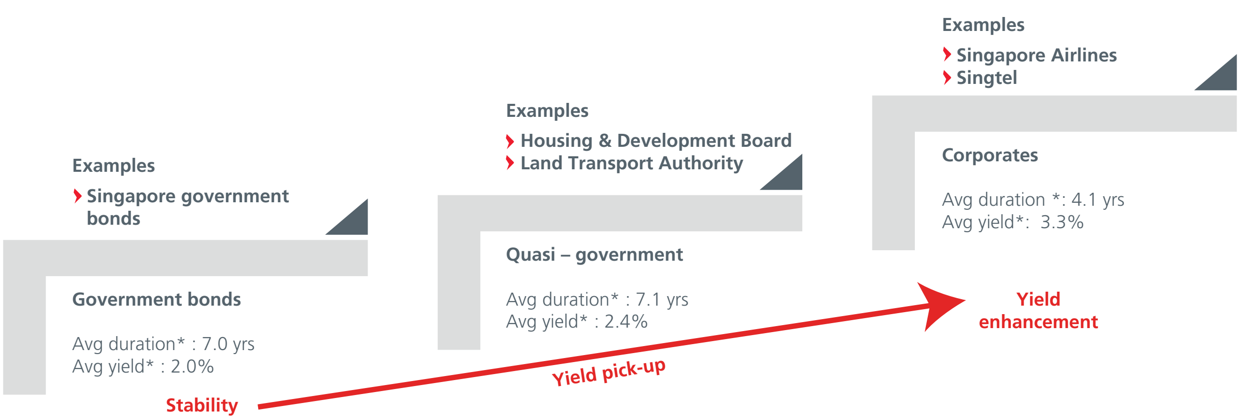


Fig. 4: A good mix of SGD bonds to enhance income with stability[5]



By diversifying across government, quasi government and corporate bonds (see Fig. 4), an active manager can provide higher yields while reducing risks. This is particularly pertinent in the current low interest rate environment, where investors may be tempted to reach for yield by buying bonds from riskier issuers.

For active managers with strong market access, they are more likely to participate in new issues, thereby enjoying greater flexibility to source for bonds that meet their yield and quality requirements.

Through careful credit selection and interest rate management, good active managers can provide investors with enhanced returns while keeping default risks in the portfolio low.

OUTLOOK

Uncertainties surrounding the US-China trade talks are likely to weigh on equity markets and keep volatility elevated. SGD bonds can play a key role in stabilising investors' portfolios while providing an attractive level of income.

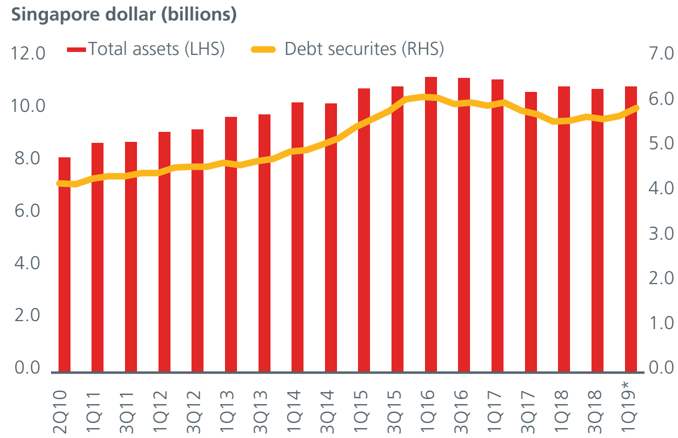
The SGD bond market will continue to grow, availing active managers with more opportunities to add value. The SGD bond market is one of the most developed markets in Asia and is becoming a natural choice for international issuers looking to raise funding outside of their home countries.

The Monetary Authority of Singapore launched the Asian Bond Grant Scheme in January 2017, which aims to broaden the issuer base in the Singapore debt market by co-funding expenses related to bond issuance for first-time issuers.

All these make the SGD bond market not only a reliable fundraising platform for issuers, but also a viable asset class for income-seeking investors.

Within the SGD bond universe, we favour corporate bonds for their higher carry. We also expect prevailing corporate bond valuations to remain supported by a strong structural demand, such as the substantial investment in debt securities from the insurance industry. See Fig. 5.

Fig. 5: Singapore's insurance industry has substantial investment in debt securities[6]



Sources: [1]Bloomberg, five years ended 16 May 2019. Strait Times Index Total Return to represent the Singapore equity market. Markit iBox ALBI Singapore index is used to track Singapore dollar bonds. [2]Morningstar Direct, from 25 May 2014 to 18 May 2019, weekly data, total returns (with income re-invested) in Singapore dollars. Risk free rate is 3-month SIBOR (Singapore Interbank Offered Rate). Singapore equities are represented by Straits Times Index, Singapore dollar bonds are represented by Markit iBoxx ALBI Singapore index. [3]Morningstar Direct Research. [4]Bloomberg, Monetary Authority of Singapore website, as at end 30 April 2019; yield-to-maturity of Markit iBoxx ALBI Singapore index, April 2019. [5]Eastspring Investments, as of end April 2019. Please note that the security (or securities) mentioned is(are) included for illustration purposes only. It should not be considered a recommendation to purchase or sell such security (or securities). The information provided herein are subject to change at the discretion of the Investment Manager without prior notice. *Based on Eastspring's calculation of yield and duration of Markit iBoxx ALBI Singapore index sub-sectors, as at 30 April 2019. [6]Monetary Authority of Singapore, 4 April 2019. *Preliminary.

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