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Boosting income streams for your golden years

With rising inflation today reducing the real rate of return of bank savings, growing your retirement nest egg is a challenge, but there are still a number of investment vehicles that prospective retirees can consider

Investing in today's environment for tomorrow's retirement is a challenge but it can be done. ST PHOTO: GIN TAY

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Investing in today's environment for tomorrow's retirement is a challenge but it can be done: Taking on more risk for higher income is one way and starting early is ideal, of course.

So what should investors take note of?

APS Asset Management founder and chief investment officer Wong Kok Hoi sets the scene: "A conservative investment strategy in today's environment must take into account at least three major macroeconomic factors: rising inflation, and related to it, rising interest rates and a possible recession."

Equities

Mr Wong favours utilities and consumer non-durables, which have good yields because dividends are less likely to be cut and the possibility of big capital losses is more remote.

But he warns that "a stock investor's focus should not purely be on dividends. Companies paying the entirety of their earnings as dividends, with substantial dividend yields of say 4 to 5 per cent or more, tend to operate mature businesses with few earnings growth prospects". In contrast, growth stocks that do not pay dividends can generate earnings growth of 20 per cent or more a year, with stock prices possibly going up by more.

Some companies also appear to trade at high dividend yields of say 10 per cent, but these can be unsustainable with cash flows deteriorating in the years ahead due to the business cycle.

Mr Wong notes: "When investing in stocks, it is best to focus on understanding the business fundamentals and the integrity of the management. A stock's dividend history and the level of dividend payout are just part of a long list of factors to evaluate whether a stock is a good buy."

APS focuses on China equities. Mr Wong reckons that "the Hong Kong-listed version of China Mobile is one of the few companies that offer a decent dividend yield of 7 per cent, and will also likely still enjoy earnings growth of close to 10 per cent a year for the next few years".

The rationale for the confidence in the earnings growth is that "as 5G penetration rates increase, and as capital expenditures taper off with the conclusion of the 4G and 5G investment cycle", APS' view is that the "5G infrastructure will last for a much longer period of time than 4G".

Singapore investors should take note of the foreign exchange risk with such overseas investments as the company's revenues and profits are sourced from China.

Reits and exchange-traded funds

Over the first half of this year, fixed-income exchange-traded funds (ETFs) recorded a 35 per cent growth in traded value compared with a year ago while real estate investment trust (Reit) ETFs grew 37 per cent over the same period.

Quite a few of the top 10 highest-dividend-paying ETFs are from these categories. They include the iShares USD Asia High Yield Bond ETF that tracks the investment results of an index composed of US dollar-denominated high-yield bonds issued by Asian governments and Asian-domiciled corporations. It had a 7.1 per cent dividend yield as at the end of June.

Another is the Lion-Phillip S-Reit ETF, which invests in high-quality Singapore Reits screened by Morningstar. The dividend yield was about 4.9 per cent.

Bonds and funds

Ms Jacquelyn Tan, UOB's head of group personal financial services, says a stable source of income can come from lower-risk dividend-paying funds as well as intermediate-duration investment-grade corporate bonds.

Some of the investment vehicles that prospective retirees can consider include:

• Investment-grade corporate bonds (credit rating BBB and above) for 3 per cent a year total returns.

• Bond funds for 4 per cent a year total returns.

• Multi-asset income funds that have exposure to both bonds and stocks for 5 per cent a year total returns.

• A diversified portfolio of multi-asset and dividend-paying equity funds at 6 per cent a year total returns.

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OCBC Bank head of wealth advisory Aaron Chwee points out that these investment-grade corporate bonds and bond funds will give a higher passive income than government bonds. Good quality bonds will be of lower risk and therefore more likely to return the principal upon maturity.

Investing in corporate bonds - not retail bonds - is usually restricted to the sophisticated investor and requires a minimum of $250,000. If that is putting too many eggs into one basket for you, then opt for unit trusts that invest primarily in bonds, Mr Chwee says.

The advantage of unit trusts is that the portfolio is diversified and a professional fund manager picks suitable bonds.

Mr Chwee also favours global multi-asset income funds which offer a broadly diversified portfolio of securities across multiple asset classes - for example, equities, fixed income, real estate and infrastructure. "The blended composition of these unit trusts allows for slightly higher yield while keeping overall portfolio volatility lower," he says.

Inflation and the long term

Given that rising inflation will reduce the real rate of return, there is little choice but to continue investing rather than let the cash remain in the bank. UOB's Ms Tan suggests that investors with a longer time horizon "can consider tapping long-term structural drivers and mega trends such as China, artificial intelligence and sustainability".

Another option is to consider defensive stocks in sectors like healthcare and consumer staples. Those with a slightly higher risk appetite can also look at US financial stocks which stand to benefit from rising interest rates, she added.

One tip, as markets are expected to remain volatile, is to invest in tranches as part of a dollar cost averaging strategy. With a longer investment horizon, and the effect of compounding, these investments can grow to a sizeable sum.

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