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For Unicorn Advised Portfolio of Unit Trusts & ETFs Clients Only

UNICORN ADVISED PORTFOLIO OF UNIT TRUSTS & ETFS
New Investment Call – 31/5/2018

Cash Portfolio

Company Name	New Allocation
China Equities Fund (s)	10%
China Bond Fund (s)	10%
Gold ETF	30%
Cash Fund	50%

For portfolios below $11k, we recommend they consist of Gold ETF and Cash Fund only.

CPF portfolio (There are no changes to the CPF portfolio for this investment call)

Company Name	Allocation
China Equities Fund (s)	10%
Short Term Duration Bond Fund (s)	90%

For portfolios below $11k, we recommend they consist of Short Term Duration Bond Fund (s) only.

SRS portfolio

Company Name	New Allocation
China Equities Fund (s)	10%
China Bond Fund (s)	10%
Cash Fund	80%

For portfolios below $11k, we recommend they consist of Cash Fund only.

Regular Savings Plan

- For Regular Savings Plan for Cash and SRS portfolio, our recommendation will be 50% in China equities fund(s) and 50% in China bond fund(s).
- For Regular Savings Plan for CPF portfolio, it will be 100% in China equities fund(s).

Why are we making this recommendation?

We are recommending a strategic allocation in China bonds for the following reasons:

1) Resilient to a significant stock market correction

We believe that a significant stock market correction is around the corner after the long ascent and conditions for the stock market ascent are now reversing. As such, we are looking for investments in asset classes that are resilient to stock market corrections.

We believe that good quality China bonds would be resilient during a stock market correction, due largely to its foreign exchange reserves of US$3.14 trillion[1]. The significant foreign exchange reserves lend creditworthiness to China's bonds.

As evidenced by the stock market correction in February 2018, China bond funds held their values, whilst Asian bond funds and Emerging Markets bond funds declined about 1 - 3% in the same period[2].

2) Attractive bond yield

Today, the yield of China government bonds stands at 3.7%, rising from 2.75% at the end of 2016[3]. We believe that the yield is sufficiently attractive for an initial allocation to this asset class. Over the last 5 years, bond yields of China 10-year government bonds have ranged between 2.75% to 4.5%[3].

Should the yields of China bonds climb significantly higher than this, we may consider further investment into China bonds.

3) Appreciation of renminbi (RMB)

We believe that China's RMB is poised to strengthen in the coming years as the currency internationalises. The stability of China's communist government also lends weight to the strength of their currency.

As the China bond fund is denominated in RMB, you will benefit when RMB appreciates.

4) Growing demand and internationalisation of the China bond market

China has made positive steps to encourage foreign investment in its local bond market.

The amount held by foreign investors in China bonds issued in China stood at about US$175 billion in 2017, or 2% of China's total domestic debt[4]. However, with the launch of HK-China Bond Connect, which allows foreign investors to trade directly in China bonds, this is expected to change. Deutsche Bank predicts that foreign investment in local China bonds will rise to 8-10% of China's total domestic debt in the next 5 years[1], which is a significant demand for China bonds.

We believe the growing demand for China bonds will translate to their price appreciation over the long term.

What are the risks?

Credit risk

We think the credit risk of bonds issued by the Chinese government and corporations have been reasonably well managed. Between 2005 to 2017, China bonds had a default rate of 0.64%, as compared to a default rate of 1.22% seen in US bonds, and a default rate of 0.78% seen in European bonds[2].

We believe that credit risk associated with investment in our recommended China bond fund is low-medium.

Interest rate risk

Our recommended China bond fund holds bonds which mature in about an average of 2 - 3 years. With bonds of a shorter duration, interest rate risk is lower as compared to long-term bond holdings. We believe that the interest rate risk associated with investment in our recommended China bond funds is low.

Currency risk

The China bond fund we are recommending to you is largely denominated in RMB and hence you are exposed to the foreign exchange movement between RMB and SGD. We think that RMB is a stable currency and hence we think this risk is low-medium.

The fund has a small portion (<10%) of their bond investments denominated in non-RMB currencies such as in USD. The fund RMB hedges their non-RMB holdings.

Conclusion

Upon considering the attractive yield and risks of investing in China bonds, we believe that a 10% allocation into a China bond fund now would be appropriate. Should bond yields climb significantly, we may increase our allocation into China bonds.

Current Allocation	New allocation
0% to China Bond Funds	10% to China Bond Funds

Sources

[1] - Reuters
[2] - iFAST
[3] - Trading Economics
[4] - The Business Times

Important Notes

The recommended funds reallocation above may result in crystallising your gains or losses from the funds that are being switched out. However, we believe that by switching out of these funds into funds that are carefully selected after our intensive research, this would mean a better long-term risk-reward proposition for your portfolio.

Investment involves risk including the possible loss of principal amount invested. Unicorn's Investing Committee monitors the recommended asset allocation closely and recommends funds after intensive research and observing market trends and macro-economic developments. However, we do not guarantee the performance of the funds and the past performance of the funds is only one of the many factors we look at; hence, it is not necessarily indicative of the future performance of the funds.